U. S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-KSB

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 1998

Commission File Number 0-16587

South Branch Valley Bancorp, Inc.
(Exact name of registrant as specified in its charter)

West Virginia	55-0672148
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

310 N. Main Street Moorefield, West Virginia	26836
(Address of principal executive offices)	(Zip Code)

(304) 538-2353
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
None	None

Securities registered pursuant to Section 12(g) of the Act:

Common
(Title of Class)

Indicate by check mark whether the registrant: (1) has filed all reports required by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K [229.405 of this chapter] is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendments to this Form 10-KSB. [X]

State issuer's revenues for its most recent fiscal year: $14,488,278

State the aggregate market value of the voting stock held by non-affiliates of the registrant. The aggregate market value shall be computed by reference to the price at which the stock was sold, or the average bid and asked prices of such stock, as of a specified date within 60 days prior to the date of filing.

Aggregate market value of voting stock	Based upon reported closing price on
$18,625,876	March 24, 1999

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

Class	Outstanding as of March 24, 1999
Common ($2.50 par value)	591,292 shares

Documents Incorporated by Reference

The following lists the documents which are incorporated by reference in the Annual Report Form 10-KSB, and the Parts and Items of the Form 10-KSB into which the documents are incorporated.

Part of Form 10-KSB

Document	into which document is Incorporated
South Branch Valley Bancorp, Inc.'s definitive Proxy Statement for the 1999 Annual Shareholders' Meeting.	Part III - Item 9, Item 10, Item 11, and Item 12

This form 10-KSB is comprised of 69 pages. The exhibit index is located on page 54.

SOUTH BRANCH VALLEY BANCORP, INC
FORM 10-KSB
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PART I.

ITEM 1. BUSINESS

Organized in 1987 as a West Virginia Corporation, South Branch Valley Bancorp, Inc. ("Company" or "South Branch") is a registered bank holding company under the Bank Holding Company Act of 1956, as amended.

At the close of business on December 31, 1987, South Branch merged its wholly owned subsidiary, South Branch Valley National Bank Inc., with South Branch Valley National Bank ("SBVNB"), a commercial bank with its principal place of business located at 310 N. Main Street, Moorefield, West Virginia.

During the first half of 1997, the Company purchased approximately 40% of the outstanding common shares of Capital State Bank, Inc ("CSB"). To facilitate the funding of this investment, the Company issued and sold 34,317 shares of its common stock at $43.50 per share to seven directors of the Company in a limited stock offering. Additionally, the Company obtained two long-term borrowings from two unaffiliated financial institutions totaling $3,500,000. On August 6, 1997, the Company entered into an Agreement and Plan of Merger with CSB to acquire the remaining 60% of its outstanding common shares. The Agreement, as amended on December 16, 1997, provided for the shareholders of CSB to receive one (1) share of the Company's common stock in exchange for each 3.95 shares of CSB stock owned. To facilitate this transaction, the Company issued a total of 183,465 shares of its common stock. On March 24, 1998 and March 25, 1998, the shareholders of CSB and the Company respectively, approved the transaction and, it was consummated at the close of business on March 31, 1998.

South Branch's business activities are conducted through its two bank subsidiaries, SBVNB and CSB. The bank subsidiaries presently account for substantially all of the consolidated assets, revenues and earnings of South Branch. SBVNB was originally chartered by the Office of the Comptroller of the Currency ("OCC") on August 15, 1883. CSB is a West Virginia banking association and was chartered on December 8, 1995. SBVNB and CSB are full service, FDIC insured institutions engaged in the commercial and retail banking business.

The Company offers a wide variety of banking services to its customers. South Branch accepts deposits and has night depositories and automated teller machines for the convenience of their customers. The Company offers its customers various deposit arrangements with a variety of maturities and yields, including non-interest bearing and interest bearing demand deposits, savings deposits, time certificates of deposit, club accounts, and individual retirement accounts.

South Branch offers a full spectrum of lending services to their customers, including commercial loans and lines of credit, residential real estate loans, consumer installment loans and other personal loans. The Company also offers credit cards, the balances of which are insignificant to total loans. Loan terms, including interest rates, loan to value ratios, and maturities are tailored as much as possible to meet the needs of the borrower. Commercial loans, which represented approximately 29.1% of total loans at December 31, 1998, are generally secured by various collateral including commercial real estate, accounts receivable and business machinery and equipment. Residential real estate loans represented approximately 51.3% of total loans as of December 31, 1998 and consist primarily of mortgages on the borrower's personal residence, and are typically secured by a first lien on the subject property. Consumer and personal loans are generally secured, often by first liens on automobiles, consumer goods or depository accounts. See Note 5 of the accompanying Consolidated Financial Statements, included in Part II, Item 7 of this Form 10-KSB, for a summary of the Company's loans at December 31, 1998 and 1997. Indirect lending represents less than 1.0% of the Company's total loans. A special effort is made to keep loan products as flexible as possible within the guidelines of prudent banking practices in terms of interest rate risk and credit risk. Company lending personnel adhere to established lending limits and authorities based on each individual's lending expertise and experience. The Company does not currently originate loans for sale.

When considering loan requests, the primary factors taken into consideration by the Company are the cash flow and financial condition of the borrower, the value of the underlying collateral, if any, and the character and integrity of the borrower. These factors are evaluated in a number of ways including an analysis of financial statements, credit reviews and visits to the borrower's place of business.

South Branch's subsidiary bank, SBVNB also serves as trustee where appointed by a court or under a private trust agreement. As trustee, SBVNB invests the trust assets and makes disbursements according to the terms and conditions of the governing trust document and state and Federal law. For the year ended December 31, 1998, fees generated from the operation of the SBVNB's Trust Department comprised less than one percent of gross revenues earned during the year.

In order to compete with other financial service providers, the Company principally relies upon personal relationships established by officers, directors, and employees with its customers, and specialized services tailored to meet its customer's needs. The Company also has a marketing program that primarily utilizes local radio and newspapers to advertise.

SUPERVISION AND REGULATION

GENERAL

South Branch, as a bank holding company, is subject to the restrictions of the BHCA, and is registered pursuant to its provisions. As a registered bank holding company, South Branch is subject to the reporting requirements of the Federal Reserve Board of Governors ("FRB"), and is subject to examination by the FRB.

The BHCA prohibits the acquisition by a bank holding company of direct or indirect ownership of more than five percent of the voting shares of any bank within the United States without prior approval of the FRB. With certain exceptions, a bank holding company is prohibited from acquiring direct or indirect ownership or control or more than five percent of the voting shares of any company which is not a bank, and from engaging directly or indirectly in business unrelated to the business of banking or managing or controlling banks.

The BHCA permits South Branch to purchase or redeem its own securities. However, Regulation Y provides that prior notice must be given to the FRB if the gross consideration for such purchase or consideration, when aggregated with the net consideration paid by the company for all such purchases or redemptions during the preceding 12 months is equal to 10 percent or more of the company's consolidated net worth. Prior notice is not required if (i) both before and immediately after the redemption, the bank holding company is well-capitalized; (ii) the bank holding company is well-managed and (iii) the bank holding company is not the subject of any unresolved supervisory issues.

The FRB, in its Regulation Y, permits bank holding companies to engage in non-banking activities closely related to banking or managing or controlling banks. Approval of the FRB is necessary to engage in these activities or to make acquisitions of corporations engaging in these activities as the FRB determines whether these acquisitions or activities are in the public interest. In addition, by order, and on a case by case basis, the FRB may approve other non-banking activities.

As a bank holding company doing business in West Virginia, South Branch is also subject to regulation by the West Virginia Board of Banking and Financial Institutions and must submit annual reports to the West Virginia Division of Banking.

Federal law restricts subsidiary banks of a bank holding company from making certain extensions of credit to the parent bank holding company or to any of its subsidiaries, from investing in the holding company stock, and limits the ability of a subsidiary bank to take its parent company stock as collateral for the loans of any borrower. Additionally, federal law prohibits a bank holding company and its subsidiaries from engaging in certain tie-in arrangements in conjunction with the extension of credit or furnishing of services.

The operations of SBVNB, as a national banking association, is subject to federal statutes and regulations which apply to national banks, and is primarily regulated by the OCC. CSB is subject to similar West Virginia statutes and regulations, and is primarily regulated by the West Virginia Division of Banking. SBVNB and CSB are also subject to regulations promulgated by the FRB and the FDIC. As members of the FDIC, the deposits of SBVNB and CSB are insured as required by federal law. Bank regulatory authorities regularly examine revenues, loans, investments, management practices, and other aspects of SBVNB and CSB. These examinations are conducted primarily to protect depositors and not shareholders. In addition to these regular examinations, South Branch's subsidiary banks each must furnish to regulatory authorities quarterly reports containing full and accurate statements of their affairs.

PERMITTED NON-BANKING ACTIVITIES

The FRB permits, within prescribed limits, bank holding companies to engage in non-banking activities closely related to banking or to managing or controlling banks. Such activities are not limited to the state of West Virginia. Some examples of non-banking activities which presently may be performed by a bank holding company are: making or acquiring, for its own account or the account of others, loans and other extensions of credit; operating as an industrial bank, or industrial loan company, in the manner authorized by state law; servicing loans and other extensions of credit; performing or carrying on any one or more of the functions or activities that may be performed or carried on by a trust company in the manner authorized by federal or state law; acting as an investment or financial advisor; leasing real or personal property; making equity or debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and the development of low income areas; providing bookkeeping services or financially oriented data processing services for the holding company and its subsidiaries; acting as an insurance agent or a broker, to a limited extent, in relation to insurance directly related to an extension of credit; acting as an underwriter for credit life insurance which is directly related to extensions of credit by the bank holding company system; providing courier services for certain financial documents; providing management consulting advice to nonaffiliated banks; selling retail money orders having a face value of not more than $1,000, traveler's checks and U. S. savings bonds; performing appraisals of real estate; arranging commercial real estate equity financing under certain limited circumstances; providing securities brokerage services related to securities credit activities; underwriting and dealing in government obligations and money market instruments; providing foreign exchange advisory and transactional services; and acting under certain circumstances, as futures commission merchant for nonaffiliated persons in the execution and clearance on major commodity exchanges of futures contracts and options.

CREDIT AND MONETARY POLICIES AND RELATED MATTERS

South Branch's subsidiary banks are affected by the fiscal and monetary policies of the federal government and its agencies, including the FRB. An important function of these policies is to curb inflation and control recessions through control of the supply of money and credit. The operations of South Branch's subsidiary banks are affected by the policies of government regulatory authorities, including the FRB which regulates money and credit conditions through open market operations in United States Government and federal agency securities, adjustments in the discount rate on member bank borrowings, and requirements against deposits and regulation of interest rates payable by member banks on time and savings deposits. These policies have a significant influence on the growth and distribution of loans, investments and deposits, and interest rates charged on loans, or paid for time and savings deposits, as well as yields on investments. The FRB has had a significant effect on the operating results of commercial banks in the past and is expected to continue to do so in the future. Future policies of the FRB and other authorities and their effect on future earnings cannot be predicted.

The FRB has a policy that a bank holding company is expected to act as a source of financial and managerial strength to each of its subsidiary banks and to commit resources to support each such subsidiary bank. Under the source of strength doctrine, the FRB may require a bank holding company to contribute capital to a troubled subsidiary bank, and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. This capital injection may be required at times when South Branch may not have the resources to provide it. Any capital loans by a holding company to any of the subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. In addition, the Crime Control Act of 1990 provides that in the event of a bank holding company's bankruptcy, any commitment by such holding company to a federal bank or thrift regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

In 1989, the United States Congress enacted the Financial Institutions Reform, Recovery and Enforcement Act ("FIRREA"). Under FIRREA depository institutions insured by the FDIC may now be liable for any losses incurred by, or reasonably expected to be incurred by, the FDIC after August 9, 1989, in connection with (i) the default of a commonly controlled FDIC-insured depository institution, or (ii) any assistance provided by the FDIC to commonly controlled FDIC-insured depository institution in danger of default. "Default" is defined generally as the appointment of a conservator or receiver and "in danger of default" is defined generally as the existence of certain conditions indicating that a "default" is likely to occur in the absence of regulatory assistance. Accordingly, in the event that any insured bank or subsidiary of South Branch causes a loss to the FDIC, other bank subsidiaries of South Branch could be liable to the FDIC for the amount of such loss.

Under federal law, the OCC may order the pro rata assessment of shareholders of a national bank whose capital stock has become impaired, by losses or otherwise, to relieve a deficiency in such national bank's capital stock. This statute also provides for the enforcement of any such pro rata assessment of shareholders of such national bank to cover such impairment of capital stock by sale, to the extent necessary, of the capital stock of any assessed shareholder failing to pay the assessment. Similarly, the laws of certain states provide for such assessment and sale with respect to the subsidiary banks chartered by such states. South Branch as the sole stockholder of its subsidiary banks, is subject to such provisions.

CAPITAL REQUIREMENTS

As a bank holding company South Branch is subject to FRB risk-based capital guidelines. The guidelines establish a systematic analytical framework that makes regulatory capital requirements more sensitive to differences in risk profiles among banking organizations, takes off-balance sheet exposures into explicit account in assessing capital adequacy, and minimizes disincentives to holding liquid, low-risk assets. Under the guidelines and related policies, bank holding companies must maintain capital sufficient to meet both a risk-based asset ratio test and leverage ratio test on a consolidated basis. The risk-based ratio is determined by allocating assets and specified off-balance sheet commitments into four weighted categories, with higher levels of capital being required for categories perceived as representing greater risk. South Branch's subsidiary banks, SBVNB and CSB are subject to substantially similar capital requirements adopted by adopted by its applicable regulatory agencies.

Generally, under the applicable guidelines, a financial institution's capital is divided into two tiers. "Tier 1", or core capital, includes common equity, noncumulative perpetual preferred stock (excluding auction rate issues) and minority interests in equity accounts of consolidated subsidiaries, less goodwill and other intangibles. "Tier 2", or supplementary capital, includes, among other things, cumulative and limited-life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan losses, subject to certain limitations, less required deductions. "Total capital" is the sum of Tier 1 and Tier 2 capital. Bank holding companies are subject to substantially identical requirements, except that cumulative perpetual preferred stock can constitute up to 25% of a bank holding company's Tier 1 capital.

Bank holding companies are required to maintain a risk-based ratio of 8%, of which 4% must be Tier 1 capital. The appropriate regulatory authority may set higher capital requirements when an institution's particular circumstances warrant.

For purposes of the leverage ratio, the numerator is defined as Tier 1 capital and the denominator is defined as adjusted total assets (as specified in the guidelines). The guidelines provide for a minimum leverage ratio of 3% for bank holding companies that meet certain specified criteria, including excellent asset quality, high liquidity, low interest rate exposure and the highest regulatory rating. Bank holding companies not meeting these criteria are required to maintain a leverage ratio which exceeds 3% by a cushion of at least 1 to 2 percent.

The guidelines also provide that bank holding companies experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. Furthermore, the FRB's guidelines indicate that the FRB will continue to consider a "tangible Tier 1 leverage ratio" in evaluating proposals for expansion or new activities. The tangible Tier 1 leverage ratio is the ratio of an institution's Tier 1 capital, less all intangibles, to total assets, less all intangibles.

On August 2, 1995, the FRB and other banking agencies issued their final rule to implement the portion of Section 305 of FDICIA that requires the banking agencies to revise their risk-based capital standards to ensure that those standards take adequate account of interest rate risk. This final rule amends the capital standards to specify that the banking agencies will include, in their evaluations of a bank's capital adequacy, an assessment of the exposure to declines in the economic value of the bank's capital due to changes in interest rates.

Failure to meet applicable capital guidelines could subject the bank holding company to a variety of enforcement remedies available to the federal regulatory authorities, including limitations on the ability to pay dividends, the issuance by the regulatory authority of a capital directive to increase capital and termination of deposit insurance by the FDIC, as well as to the measures described under the "Federal Deposit Insurance Corporation Improvement Act of 1991" as applicable to undercapitalized institutions.

As of December 31, 1998, the regulatory capital ratios of South Branch and its bank subsidiaries are set forth in the table in Note 13 of the notes of the accompanying consolidated financial statements

FEDERAL DEPOSIT INSURANCE CORPORATION IMPROVEMENT ACT OF 1991

In December, 1991, Congress enacted the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), which substantially revised the bank regulatory and funding provisions of the Federal Deposit Insurance Corporation Act and made revisions to several other banking statues.

FDICIA establishes a new regulatory scheme, which ties the level of supervisory intervention by bank regulatory authorities primarily to a depository institution's capital category. Among other things, FDICIA authorizes regulatory authorities to take "prompt corrective action" with respect to depository institutions that do not meet minimum capital requirements. FDICIA establishes five capital tiers: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically under capitalized.

By regulation, an institution is "well-capitalized" if it has a total risk-based capital ratio of 10% or greater, a Tier 1 risk-based capital ratio of 6% or greater and a Tier 1 leverage ratio of 5% or greater and is not subject to a regulatory order, agreement or directive to meet and maintain a specific capital level for any capital measure. The banking subsidiaries of South Branch were "well capitalized" institutions as of December 31, 1998. As well-capitalized institutions, SBVNB and CSB are permitted to engage in a wider range of banking activities, including among other things, the accepting of "brokered deposits," and the offering of interest rates on deposits higher than the prevailing rate in their respective markets.

Another requirement of FDICIA is that federal banking agencies must prescribe regulations relating to various operational areas of banks and bank holding companies. These include standards for internal audit systems, loan documentation, information systems, internal controls, credit underwriting, interest rate exposure, asset growth, compensation, a maximum ratio of classified assets to capital, minimum earnings sufficient to absorb losses, a minimum ratio of market value to book value for publicly traded shares and such other standards as the agency deems appropriate.

REIGLE-NEAL INTERSTATE BANKING BILL

In 1994, Congress passed the Reigle-Neal Interstate Banking Bill (the "Interstate Bill"). The Interstate Bill permits certain interstate banking activities through a holding company structure, effective September 30, 1995. It permits interstate branching by merger effective June 1, 1997 unless states "opt-in" sooner, or "opt-out" before that date. States may elect to permit de novo branching by specific legislative election. In March, 1996, West Virginia adopted changes to its banking laws so as to permit interstate banking and branching to the fullest extent permitted by Interstate Bill. The Interstate Bill will permit consolidation of banking institutions across state lines and, perhaps, de novo entry. As its provisions become effective, it is likely that the resulting restructurings and interstate activities will result in the realization of economies of scale within those institutions with entities in more than one state. One result could be increased competitiveness, due to the realization of economies of scale and, where permitted, due to de novo market entrants.

COMMUNITY REINVESTMENT ACT

Bank holding companies and their subsidiary banks are also subject to the provisions of the Community Reinvestment Act of 1977 ("CRA"). Under the CRA, the Federal Reserve Board (or other appropriate bank regulatory agency) is required, in connection with its examination of a bank, to assess such bank's record in meeting the credit needs of the communities served by that bank, including low and moderate income neighborhoods. Further such assessment is also required of any bank holding company which has applied to (i) charter a national bank, (ii) obtain deposit insurance coverage for a newly chartered institution, (iii) establish a new branch office that will accept deposits, (iv) relocate an office, or (v) merge or consolidate with, or acquire the assets or assume the liabilities of a federally-regulated financial institution. In the case of a bank holding company applying for approval to acquire a bank or other bank holding company, the Federal Reserve Board will assess the record of each subsidiary of the applicant bank holding company, and such records may be the basis for denying the application or imposing conditions in connection with approval of the application. On December 8, 1993, the federal regulators jointly announced proposed regulations to simplify enforcement of the CRA by substituting the present twelve categories with three assessment categories for use in calculating CRA ratings (the "December 1993 Proposal"). In response to comments received by the regulators regarding the December 1993 Proposal, the federal bank regulators issued revised CRA proposed regulations on September 26, 1994 (the "Revised CRA Proposal"). The Revised CRA Proposal, compared to the December 1993 Proposal, would essentially broaden the scope of CRA performance examinations and more explicitly consider community development activities. Moreover, in 1994, the Department of Justice, became more actively involved in enforcing fair lending laws.

In the most recent CRA examinations by the applicable bank regulatory authorities, South Branch's bank subsidiaries were given "satisfactory" or better CRA ratings.

DEPOSIT ACQUISITION LIMITATION

Under West Virginia banking law, an acquisition or merger is not permitted if the resulting depository institution or its holding company, including any depository institutions affiliated therewith, would assume additional deposits to cause it to control deposits in the State of West Virginia in excess of twenty five percent (25%) of such total amount of all deposits held by insured depository institutions in West Virginia. This limitation may be waived by the Commissioner of Banking for good cause shown.

COMPETITION

The Company competes primarily with numerous other banks and financial institutions within its primary market area of the Eastern Panhandle and South Central counties of West Virginia. It can be expected that with the liberalization of the branch banking laws in West Virginia, additional financial institutions may compete with the Company. South Branch takes an aggressive competitive posture, and intends to continue vigorously competing for its share of the market within its service area by offering competitive rates and terms on both loans and deposits.

EMPLOYEES

At December 31, 1998, the Company employed 72 full-time equivalent employees.

ITEM 2. PROPERTIES

In 1974 the SBVNB acquired 5.82 acres of land located on the west side of U.S. Route 220 on Main Street in Moorefield, West Virginia. On June 29, 1976 SBVNB received the approval of the Office of the Comptroller of the Currency to locate of its main office to this site. This is the present location of the SBVNB's and the Company's principal offices. In April 1994 SBVNB acquired approximately one acre of real estate on the west side of U.S. Route 220 adjoining the main office. During 1998, SBVNB acquired an additional 5 acres of the land adjoining this site.

On April 5, 1983 the SBVNB acquired property located in the town of Mathias, West Virginia. Since December 28, 1984 the SBVNB has operated its Mathias branch bank from this site.

By deeds dated May 31, 1986 and July 14, 1986 the SBVNB acquired two parcels of land located on the east side of U.S. Route 220 in the town of Franklin, West Virginia. On October 3, 1986 the SBVNB received preliminary approval from the Office of the Comptroller of the Currency to establish a branch bank at this location. SBVNB's Franklin branch was opened for banking operations on January 1, 1987.

During 1995, SBVNB acquired a parcel of land and branch office located on the north side of U.S. Route 220 in the town of Petersburg, West Virginia. This property was purchased from Blue Ridge Bank and began operating as a branch of SBVNB on November 15, 1995.

In conjunction with the acquisition of CSB in March 1998, the Company acquired CSB's banking facility located in South Ridge Centre in Charleston, West Virginia. South Ridge is a large shopping center complex on U.S. Route 119 approximately eight miles south of the Charleston downtown area. CSB's facility opened on December 16, 1995, and is constructed on land leased for an initial 50 year term expiring in 2045.

ITEM 3. LEGAL PROCEEDINGS

South Branch is involved in various pending legal proceedings, all of which are regarded by management as normal litigation incident to the business of banking and are not expected to have a materially adverse effect on the business or financial condition of the Company.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SHAREHOLDERS

No matters were submitted during the fourth quarter of 1998 to a vote of Company shareholders.

PART II.

ITEM 5. MARKET FOR REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company acts as its own registrar and transfer agent. During 1998, its shares were not publicly traded on any exchange or over the counter market. Shares of the Company's common stock were occasionally bought and sold by private individuals, firms or corporations. In many instances, the Company did not have knowledge of the purchase price or the terms of the purchase. No definitive records of bids and ask or sale prices were available.

Beginning on January 6, 1999, quotation of South Branch's common stock began on the OTC Bulletin Board under the symbol "SBVB".

The approximate number of stockholders of record for South Branch's common stock as of March 19, 1999 was 1,446.

The following sets forth quarterly cash dividends declared per share for the prior two years.

	Quarterly Common Stock Dividend	
Quarter	1998	1997
First	$ -	$ -
Second	.44	.41
Third	-	-
Fourth	.45	.43

Dividends paid by South Branch to its stockholders are based on dividends it receives from its subsidiary banks. The ability of the bank subsidiaries to pay dividends to South Branch is subject to certain limitations of the national banking laws. In general, these limitations provide that no bank can pay dividends if the total of all dividends, including any proposed dividend declared by a bank in any calendar year, exceeds net income for that year when combined with net income for the preceding two years, less dividends for all three years. This restriction may be waived if the approval of the applicable bank regulatory authorities is obtained for such distribution.

Additional information with regard to dividend restrictions is included in Note 13 of the Notes to Consolidated Financial Statements included on pages 46 through 47 under Part II, Item 7 of this filing.

Cash dividends rose 6.0% to $.89 per share in 1998. It is the intention of management and the Board of Directors to continue to pay dividends on similar schedule during 1998. However, future cash dividends will depend on the earnings, financial condition and the business of the bank subsidiaries, as well as general economic conditions; however, management is not presently aware of any reason why dividend payments should not continue.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS AND RELATED STATISTICAL DISCLOSURES

INTRODUCTION AND SUMMARY

The following is management's discussion and analysis of the financial condition and financial results of operations for South Branch Valley Bancorp, Inc. ("Company" or "South Branch") and its wholly owned subsidiaries, South Branch Valley National Bank ("SBVNB") and Capital State Bank, Inc. ("CSB") as of December 31, 1998. This discussion may contain forward looking statements based on management's expectations and actual results may differ materially. Since the primary business activities of South Branch Valley Bancorp, Inc. are conducted through its wholly owned bank subsidiaries, the following discussion focuses primarily on the financial condition and operations of SBVNB and CSB. All amounts and percentages have been rounded for this discussion. This discussion and analysis should be read in conjunction with the consolidated financial statements and accompanying notes thereto of the Company as of December 31, 1998 and for each of the three years then ended.

ACQUISITION

At the close of business March 31, 1998, South Branch acquired 60% of the outstanding common stock of CSB, a Charleston, West Virginia state chartered bank with total assets approximating $44 million at the time of acquisition, in exchange for 183,465 shares of South Branch's common stock. South Branch had previously acquired 40% of CSB's outstanding common stock during 1997. This acquisition was accounted for using the purchase method of accounting, and accordingly, the assets and liabilities and results of operations of CSB are reflected in the Company's consolidated financial statements beginning April 1, 1998. Refer to Note 2 of the accompanying consolidated financial statements for additional information regarding this acquisition.

RESULTS OF OPERATIONS

EARNINGS SUMMARY

Net income for the three years ended December 31, 1998, 1997, and 1996, was $1,733,000, $1,520,000, and $1,490,000, respectively. On a per share basis, net income was $3.16 in 1998 compared to $3.83 in 1997, and $3.94 in 1996. Return on average total assets for the year ended December 31, 1998 was 0.98% compared to 1.15% in 1997 and 1.27% in 1996. Return on average equity was 7.41% in 1998 compared to 11.09% in 1997. A summary of the significant factors influencing the Company's results of operations and related ratios is included in the following discussion.

NET INTEREST INCOME

The major component of the South Branch's net earnings is net interest income, which is the excess of interest earned on earning assets over the interest expense incurred on interest bearing sources of funds. Net interest income is affected by changes in volume, resulting from growth and alterations of the balance sheet's composition, fluctuations in interest rates and maturities of sources and uses of funds. Management seeks to maximize net interest income through management of its balance sheet components. This is accomplished by determining the optimal product mix with respect to yields on assets and costs of funds in light of projected economic conditions, while maintaining portfolio risk at an acceptable level.

Net interest income, adjusted to a fully tax equivalent basis, totaled $7,001,000, $5,346,000 and $5,059,000 for the years ended December 31, 1998, 1997, and 1996 respectively resulting in a net interest margin of 4.3% for 1998 compared to 4.4% and 4.6% for 1997 and 1996, respectively. The net interest margin recognizes earning asset growth by expressing net interest income as a percentage of total average earning assets. Lower yields on interest earning assets continued to negatively impact the Company's net interest margin. In 1998, the yield on interest earning assets decreased 20 basis points from 8.8% in 1997 to 8.6% in 1998, primarily due to the acquisition of CSB which had a lower yield on interest earning assets than that of SBVNB, while the cost of interest bearing liabilities remained unchanged at 5.0% during the same periods. The spread between interest earning assets and interest bearing liabilities could continue to contract, thus negatively impacting the Company's net interest income in 1999. Management continues to monitor the net interest margin through simulation and GAP analyses to minimize the potential for any significant negative impact. See the Interest Rate Risk Management section for further discussion of the impact of changes in market interest rates could have on the Company.

Net interest income on a fully tax equivalent basis, average balance sheet amounts, and corresponding average yields on earning assets and costs of interest bearing liabilities for the years 1998, 1997 and 1996 are presented in Table I. Table II presents, for the periods indicated, the changes in interest income and expense attributable to (a) changes in volume (changes in volume multiplied by prior period rate) and (b) changes in rate (change in rate multiplied by prior period volume). Changes in interest income and expense attributable to both rate and volume have been allocated between the factors in proportion to the relationship of the absolute dollar amounts of the change in each.

As identified in Table II, the change in net interest margin from 1998 to 1997 was primarily attributed to the change in volume of certain interest bearing assets and liabilities, the reasons which are presented later in this discussion under the appropriate balance sheet section.

PROVISION FOR LOAN LOSSES

The provision for loan losses represents management's determination of the amount necessary to be charged against the current period's earnings in order to maintain the allowance for loan losses at a level which is considered adequate in relation to the estimated risk inherent in the loan portfolio. The provision for loan losses for each of the years ended December 31, 1998, 1997 and 1996 totaled $270,000, $155,000 and $95,000, respectively. As further discussed in the Loan Portfolio and Risk Elements section of this analysis, increases in South Branch's provision for loan losses are primarily attributed to the acquisition of CSB and the Company's continued, strong loan growth. An analysis of the components comprising the allowance for loan losses for the years ended December, 1998, 1997 and 1996, including charge offs and recoveries within each significant loan classification, is included in Note 6 of the accompanying consolidated financial statements.

NONINTEREST INCOME

Noninterest income totaled $609,000, $525,000 and $457,000 or 4.2%, 4.7%, and 4.5% of total income for each of the years ended December 31, 1998, 1997, and 1996, respectively. Excluding gains on the sale of Bank premises, equipment and other assets recognized in 1998 and 1997, total other income increased approximately $157,000 or 36.1% in 1998, as compared to 1997. The most significant items contributing to this increase was service fee income, which increased $151,000 from approximately $280,000 to $431,000, or 53.9%, which resulted primarily from a change in SBVNB's deposit fee structure and the acquisition of CSB.

NONINTEREST EXPENSE

Noninterest expense totaled $4,476,000, $3,342,000 and $3,156,000 or 38.0%, 37.5% and 39.4% of total expense for each of the years ended December 31, 1998, 1997, and 1996, respectively. Total noninterest expense increased $1,134,000 or 33.9% from 1997 to 1998. Substantially all of this increase resulted from the $940,000 in noninterest expenses that Capital State incurred from the date of its acquisition on April 1, 1998 through December 31, 1998.

INCOME TAX EXPENSE

Income tax expense (benefit) for the three years ended December 31, 1998, 1997, and 1996 totaled $967,000, $691,000 and $643,000, respectively. Refer to Note 10 of the accompanying consolidated financial statements for further information and additional discussion of the significant components influencing the Company's effective income tax rates.

TABLE I - AVERAGE DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY, INTEREST EARNINGS & EXPENSES, AND AVERAGE RATES
(In thousands of dollars)

	1998			1997			1996		
	Average Balances	Earnings/ Expense	Yield Rate	Average Balances	Earnings/ Expense	Yield Rate	Average Balances	Earnings/ Expense	Yield Rate
ASSETS									
Interest earning assets									
Loans, net of unearned									
interest (1)	$123,003	$11,437	9.3%	$90,082	$8,558	9.5%	$76,797	$7,552	9.8%
Securities									
Taxable	27,567	1,813	6.6%	23,572	1,541	6.5%	26,557	1,711	6.4%
Tax-exempt (2)	6,213	486	7.8%	6,005	477	7.9%	4,757	386	8.1%
Interest bearing deposits									
with other banks	1,056	72	6.8%	1,437	97	6.8%	1,869	125	6.7%
Federal funds sold	4,992	236	4.7%	1,388	80	5.8%	892	49	5.5%
Total interest earning assets	162,831	14,044	8.6%	122,484	10,753	8.8%	110,872	9,823	8.9%
Noninterest earning assets									
Cash and due from banks	3,684			2,752			2,419		
Bank premises and equipment	4,634			3,121			3,155		
Other assets	6,653			4,773			1,298		
Allowance for loan losses	(1,190)			(852)			(861)		
Total assets	$176,612			$ 132,278			$116,883		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Liabilities									
Interest bearing liabilities									
Interest bearing									
demand deposits	$24,085	$830	3.4%	$18,725	$579	3.1%	$19,761	$669	3.4%
Savings deposits	15,730	502	3.2%	13,349	424	3.2%	15,048	523	3.5%
Time deposits	82,479	4,760	5.8%	62,307	3,604	5.8%	57,756	3,398	5.9%
Short-term borrowings	5,371	232	4.3%	5,685	256	4.5%	1,579	68	4.3%
Long-term borrowings	13,004	719	5.5%	7,831	544	6.9%	1,803	106	5.9%
	140,669	7,043	5.0%	107,897	5,407	5.0%	95,947	4,764	5.0%
Noninterest bearing liabilities									
Demand deposits	11,012			9,213			8,532		
Other liabilities	1,533			1,468			914		
Total liabilities	153,214			118,578			105,393		
Shareholders' equity	23,398			13,700			11,490		
Total liabilities and shareholders' equity	$176,612			$132,278			$116,883		
NET INTEREST EARNINGS		$7,001			$5,346			$5,059	
NET INTEREST YIELD ON EARNING ASSETS			4.3%			4.4%			4.6%

(1) - For purposes of this table, non-accrual loans are included in average loan balances. Included in interest and fees on loans are loan fees of $324,000, $173,000 and $181,000 for the years ended December 31, 1998, 1997 and 1996, respectively.

(2) - For purposes of this table, interest income on tax-exempt securities has been adjusted assuming an effective combined Federal and state tax rate of 34% for all years presented. The tax equivalent adjustment results in an increase in interest income of $165,000, $162,000 and $131,000 for the years ended December 31, 1998, 1997 and 1996, respectively.

TABLE II - CHANGES IN INTEREST MARGIN ATTRIBUTABLE TO RATE AND VOLUME
(In thousands of dollars)

	1998 VERSUS 1997			1997 VERSUS 1996		
	Increase (Decrease) Due to Change in:			Increase(Decrease) Due to Change in:		
	Volume	Rate	Net	Volume	Rate	Net
Interest earned on:						
Loans	$3,065	$(186)	$2,879	$1,269	$(263)	$1,006
Securities						
Taxable	263	9	272	(193)	23	(170)
Tax-exempt	17	(8)	9	99	(8)	91
Interest bearing deposits with other banks	(26)	1	(25)	(29)	1	(28)
Federal funds sold	173	(17)	156	28	3	31
Total interest earned on interest earning assets	3,492	(201)	3,291	1,174	(244)	930
Interest paid on:						
Interest bearing demand deposits	180	71	251	(36)	(54)	(90)
Savings deposits	76	2	78	(62)	(37)	(99)
Time deposits	1,164	(8)	1,156	264	(58)	206
Short-term borrowings	(14)	(10)	(24)	185	3	188
Long-term borrowings	303	(128)	175	415	23	438
Total interest paid on interest bearing liabilities	1,709	(73)	1,636	766	(123)	643
Net interest income	$1,783	$(128)	$1,655	$408	(121)	287

CHANGES IN FINANCIAL POSITION

Total average assets for the year ended December 31, 1998 were $176,612,000 an increase of 33.5% over 1997's average of $132,278,000. This increase in total average assets is primarily attributable to the CSB acquisition and growth in deposits and borrowings and are detailed below in the discussions of changes in significant components of the Company's balance sheet between December 31, 1997 and December 31, 1998. The Company's total average interest earning assets, expressed as a percentage of total assets, remains high, although this ratio has decreased slightly to 92.2% for 1998 as compared to 92.6% for 1997.

SECURITIES

Securities comprised approximately 16.3% of total assets at December 31, 1998 compared to 19.6% at December 31, 1997. All securities are classified as available for sale to provide management with flexibility to better manage its balance sheet structure and react to asset/liability management issues as they arise. Average securities approximated $33,780,000 for 1998 or 14.2% more than 1997's average of $29,577,000. Refer Note 4 of the accompanying consolidated financial statements for details of amortized cost, the fair values, unrealized gains and losses as well as the security classifications by type.

At December 31, 1998, the Company did not own securities of any one issuer that exceeded ten percent of shareholders' equity. The maturity distribution of the securities portfolio at December 31, 1998, together with the weighted average yields for each range of maturity, are summarized in Table III. The stated average yields are actual yields and are not stated on a tax equivalent basis.

TABLE III - SECURITIES MATURITY ANALYSIS
(At amortized cost, in thousands of dollars)

	Within one year		After one but within five years		After five but within ten years		After ten years	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for sale								
U. S. Treasury securities	$1,499	6.6%	$1,491	6.3%	$ -	-	$ -	-
U. S. Government agencies and corporations	1,498	6.5%	6,477	6.1%	4,723	6.3%	-	-
Small Business Administration guaranteed loan participation certificates	394	6.4%	579	6.4%	-	-	-	-
Mortgage backed securities - U. S. Government agencies and corporations	2,916	6.7%	3,418	6.4%	-	-	-	-
State and political subdivisions	413	3.5%	1,827	4.1%	1,834	4.9%	2,174	5.2%
Other	250	7.0%	-	-	-	-	1,408	6.5%
	$ 6,970	6.0%	$13,792	5.7%	$6,557	5.9%	$3,582	5.7%

LOAN PORTFOLIO

The following table depicts loan balances at December 31, 1998 and 1997 by types along with their respective percentage of total loans outstanding.

	(In thousands of dollars) 1998		1997	
	Amount	Percent of Total	Amount	Percent of Total
Commercial, financial and agricultural	$41,957	29.1%	$30,325	32.4%
Real estate - construction	1,801	1.2%	144	0.2%
Real estate - mortgage	73,886	51.3%	42,640	45.6%
Installment loans to individuals (net of unearned interest)	26,089	18.1%	19,890	21.3%
Other	409	0.3%	469	0.5%
Total loans	144,142	100.0%	93,468	100.0%
Less allowance for loan losses	1,372		895	
Loans, net	$142,770		$92,573	

Total net loans averaged $123,003,000 in 1998 and comprised 69.6% of total average assets compared to $90,082,000 or 68.1% of total average assets during 1997. This increase in the dollar volume of loans is primarily attributable to the CSB acquisition and to continuation of the Company's strategy which began in 1996 to more aggressively expand the Company's commercial and real estate loan portfolios.

Refer to Note 5 of the accompanying consolidated financial statements for the Company's loan maturities and a discussion of the Company's adjustable rate loans as of December 31, 1998.

In the normal course of business, the Company makes various commitments and incurs certain contingent liabilities which are disclosed in Note 12 to the accompanying consolidated financial statements but not reflected in the accompanying consolidated financial statements. There have been no significant changes in these type of commitments and contingent liabilities and the Company does not anticipate any material losses as a result of these commitments.

RISK ELEMENTS

The following table presents a summary of restructured or non-performing loans for each of the three years ended December 31, 1998, 1997 and 1996.

	(In thousands of dollars) December 31, 1998	1997	1996
Nonaccrual loans	$297	$ 142	$343
Accruing loans past due 90 days or more	355	96	324
Restructured loans	-	55	55
Total	$ 652	$ 293	$722
Percentage of total loans	0.5%	0.3%	0.9%

The increase in non-performing loans from year 1997 to 1998 is not deemed significant relative to the growth in the size of the loan portfolio, as total nonaccrual and restructured loans as a percentage of total outstanding loans have remained at a low level of less than 1 percent for each of the three years presented. Refer to Note 5 of the accompanying consolidated financial statements for additional discussion of non-accrual loans and to Note 6 for a discussion of impaired loans which are included in the above balances..

The Company's subsidiary banks, on a quarterly basis, perform a comprehensive loan evaluation which encompasses the identification of all potential problem credits which are included on an internally generated watch list. The identification of loans for inclusion on the watch list is facilitated through the use of various sources, including past due loan reports, previous internal and external loan evaluations, classified loans identified as part of regulatory agency loan reviews and reviews of new loans representative of current lending practices within the Bank. Once this list is reviewed to ensure it is complete, the credit review department reviews the specific loans for collectibility, performance and collateral protection. In addition, a grade is assigned to the individual loans utilizing internal grading criteria, which is somewhat similar to the criteria utilized by the Bank's primary regulatory agency. Based on the results of these reviews, specific reserves for potential losses are identified and the allowance for loan losses is adjusted appropriately through a provision for loan losses. While there may be some loans or portions of loans identified as potential problem credits which are not specifically identified as either non-accrual or accruing loans past due 90 or more days, they are considered by management to be insignificant to the overall disclosure and are, therefore, not specifically quantified within this discussion. In addition, management feels these additional loans do not represent or result from trends or uncertainties which management reasonably expects will materially impact future operating results, liquidity or capital resources. Also, these loans do not represent material credits about which management is aware of any information which would cause the borrowers to not comply with the loan repayment terms.

Specific reserves are allocated to non-performing loans based on the quarterly evaluation of expected loan loss reserve requirements as determined by Company management. In addition, a portion of the reserve is determined through the use of loan loss experience factors which do not provide for identification of specific potential problem loans. As noted above, some of the loans, which are not deemed significant, are included in the watch list of potential problem loans and have specific reserves allocated to them.

At December 31, 1998 and 1997 respectively, the allowance for loan losses represented 1.0% and 1.0% of gross loans or $1,372,000 and $895,000 and was considered adequate to cover inherent losses in the subsidiary bank's loan portfolio as of the respective evaluation date. The Company maintains an allowance for loan losses at a level considered adequate to provide for losses that can be reasonably anticipated. The Company performs a quarterly evaluation of the loan portfolio to determine its adequacy. The evaluation is based on assessments of specifically identified loans, loss experience factors, current and anticipated economic conditions and other factors to identify and estimate inherent losses from homogeneous pools of loans.

The allocated portion of the subsidiary bank's allowance for loan losses is established on a loan-by-loan and pool-by-pool basis. The unallocated portion is for inherent losses that probably exist as of the evaluation date, but which have not been specifically identified by the processes used to establish the allocated portion due to inherent imprecision in the objective processes management utilizes to identify probable and estimable losses. This unallocated portion is subjective and requires judgement based on various qualitative factors in the loan portfolio and the market in which the Company operates. At December 31, 1998 and 1997, respectively, the unallocated portion of the allowance approximated $86,000 and $67,000, or 6.3% and 7.5% of the total allowance. This unallocated portion of the allowance was considered necessary based on consideration of the known risk elements in certain pools of loans in the loan portfolio and management's assessment of the economic environment in which the Company operates. More specifically, while loan quality remains good, the subsidiary banks have typically experienced greater losses within certain homogeneous loan pools when the Company's market area has experienced economic downturns or other significant native factors or trends, such as increases in bankruptcies, unemployment rates or past due loans.

Table IV below presents an allocation of the expected allowance for loan losses by major loan type.

TABLE IV - ALLOCATION OF THE ALLOWANCE FOR LOAN LOSSES
(In thousands of dollars)

	1998		1997		1996	
	Amount	Percent of loans in each category to total loans	Amount	Percent of loans in each category to total loans	Amount	Percent of loans in each category to total loans
Commercial,financial						
and agricultural	$ 377	29.1%	$ 182	32.4%	$ 182	32.9%
Real estate	363	52.5%	300	45.8%	303	44.1%
Installment	539	18.1%	339	21.3%	294	22.3%
Other	7	0.3%	7	0.5%	11	0.7%
Unallocated	86	-	67	-	68	-
	$1,372	100.0%	$ 895	100.0%	$ 858	100.0%

At December 31, 1998, the Company had approximately $85,000 in other real estate owned which was obtained as the result of foreclosure proceedings and $12,000 in other repossessed assets which was obtained as the result of auto repossessions. These repossessions have been insignificant throughout 1998 and management does not anticipate any material losses on any of the items currently held in other real estate owned or other repossessed assets.

DEPOSITS

Total deposits at December 31, 1998 increased approximately $39,388,000 or 36.8% compared to December 1997. Average deposits increased approximately $27,913,000 or 29.6% during 1998. This growth was primarily the result of the acquisition of CSB.

See Note 8 of the accompanying consolidated financial statements for a maturity distribution of time deposits as of December 31, 1998.

BORROWINGS

Lines of Credit: The Company has available lines of credit from the Federal Home Loan Bank of Pittsburgh which totaled $28,264,000 at December 31, 1998. Management uses this line to make additional funds available to customers in the form of loans at competitive rates. Funds acquired through this program are reflected on the consolidated balance sheet as part of short-term borrowings or long-term borrowings, depending on the repayment terms of the debt agreement. Refer to Note 9 of the accompanying consolidated financial statements for additional discussion of short-term borrowings activity and long-term borrowings.

Other lines of credit available, but unused, to the Company through correspondent banks totaled $10,000,000 as of December 31, 1998.

Short-term Borrowings: Total short-term borrowings decreased $2,501,000 or 35.0% from $7,145,000 at December 31, 1997 to $4,644,000 at December 31, 1998. See Note 9 of the accompanying consolidated financial statements for a discussion of short-term borrowings.

Long-term Borrowings: The Company's long-term borrowings of $16,469,000 at December 31, 1998, compared to $10,396,000 at December 31, 1997, consisted entirely of funds borrowed on available lines of credit from the Federal Home Loan Bank to fund fixed rate local mortgage growth and specific commercial loan projects. Refer to Note 9 of the accompanying consolidated financial statements for a discussion of long-term borrowings.

LIQUIDITY

Liquidity in commercial banking can be defined as the ability to satisfy customer loan demand and meet deposit withdrawals while maximizing net interest income. The Company uses ratio analysis to monitor the changes in its sources and uses of funds so that an adequate liquidity position is maintained. Liquidity was available through cash, due from banks, Federal funds sold, securities and interest bearing deposits with other banks maturing within one year and totaled approximately $16,896,000 and $11,799,000, or 8.5% and 8.4%of total assets at December 31, 1998 and 1997, respectively. Secondary sources of liquidity are provided by all remaining available for sale securities, Federal funds purchased, Federal Home Loan Bank lines of credit, and correspondent banks lines of credit. Management believes that the liquidity of the Company is adequate and foresees no demands or conditions that would adversely affect it.

INTEREST RATE RISK MANAGEMENT

The principal objective of asset/liability management is to minimize interest rate risk, which is the vulnerability of the Company's net interest income to changes in interest rates and manage the ratio of interest rate sensitive assets to interest rate sensitive liabilities within specified maturities or repricing dates. The Company's actions in this regard are taken under the guidance of the subsidiary banks' asset/liability management committees, which are comprised of members of the Banks' senior management and members of each respective institution's boards of directors. The Company's asset/liability management committees actively formulate the economic assumptions that the Company uses in its financial planning and budgeting process and establishes policies which control and monitor the banks' sources, uses and prices of funds.

Some amount of interest rate risk is inherent and appropriate to the banking business. Several techniques are available to monitor and control the level of interest rate risk. The Company regularly performs modeling to project the potential impact of future interest rate scenarios on net interest income. Through such simulation analysis, interest rate risk is maintained within established policy limits. Based upon the present mix of assets and liabilities and management's assumptions with respect to growth and repricing, no significant impact on the Company's 1999 net interest margin is expected given a 200 basis point change, either upward or downward, in interest rates during 1999.

Another means of analyzing an institution's interest rate risk is by monitoring its interest rate sensitivity "gaps." An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity "gap' is defined as the difference between interest earning assets and interest bearing liabilities maturing or repricing within a given time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds interest rate sensitive assets. During a period of falling interest rates, a positive gap would tend to adversely affect net interest income, while a negative gap would tend to result in an increase in net interest income. During a period of rising interest rates, a positive gap would tend to result in an increase in net interest income while a negative gap would tend to affect net interest income adversely.

Table V sets forth the Company's interest rate sensitivity gaps within the one year time horizon computed based upon contractual repricings and maturities at December 31, 1998. As presented in the table, the Company has a one year cumulative negative interest sensitivity gap of $59 million (or 33.0% of total earning assets). However, included within the one year time period are $42 million of interest bearing demand and savings deposits which on a contractual basis are immediately repriceable. The actual repricing of these deposits tends to lag well behind movements in market interest rates. Accordingly, the sensitivity of such core deposits to changes in market interest rate may differ significantly from their contractual terms. If interest bearing demand and savings deposits are assumed to reprice beyond the one year time horizon, the Company's one year cumulative interest rate sensitivity gap at December 31, 1998 would be a negative $17 million or just 9.5% of interest earning assets.

TABLE V: ASSET & LIABILITY RATE SENSITIVITY ANALYSIS, DECEMBER 31, 1998
(In Thousands of Dollars)

	Maturing or Repricing Within			
	0-90 Days	91-180 Days	181-365 Days	Total 1 Year
Interest earning assets:				
Loans	$16,892	$11,117	$9,533	$37,542
Taxable securities	499	1,250	1,498	3,247
Mortgage-backed securities	1,716	797	797	3,310
Tax-exempt securities	-	161	252	413
	19,107	13,325	12,080	44,512
Interest bearing liabilities:				
Certificates of deposit	14,868	17,592	29,083	61,543
Savings deposits	14,749	-	-	14,749
Interest bearing demand deposits	27,511	-	-	27,511
	57,128	17,592	29,083	103,803
Static Interest Sensitivity Gap	$(38,021)	$(4,267)	$(17,003)	$(59,291)
Cumulative Gap	$(38,021)	$(42,288)	$(59,291)	
Gap/Total Earning Assets				-33.0%
Gap/Total Earning Assets (excluding savings & demand deposits)				-9.5%

CAPITAL RESOURCES

The capital position of South Branch Valley Bancorp, Inc. has shown consistent growth during the past three years. Stated as a percentage of total assets, the Company's equity ratio was 12.5%, 10.7%, and 10.1% at December 31, 1998, 1997 and 1996 respectively. These increases can be attributed to a strong earnings base during the past three years combined with the impact of the acquisition of CSB in 1998. The Company's risk weighted tier I capital, total capital and leverage capital ratios were approximately 17.3%, 18.4% and 11.5%, respectively, at December 31, 1998 which is considered well capitalized under regulatory guidelines for prompt corrective action provisions. The Company's subsidiary banks are also subject to minimum capital ratios as further discussed in Note 13 of the accompanying consolidated financial statements.

The percentage of earnings retained by the Company to fund future growth has not significantly changed during the three years ended December 31, 1998. Cash dividends per share rose 5.9% to $.89 in 1998 compared to $.84 in 1997, representing dividend payout ratios of 28.2% and 21.9% for 1998 and 1997, respectively. It is the intention of management and the Board of Directors to continue to pay dividends on a similar schedule during 1999. Future cash dividends will depend on the earnings, financial condition and the business of the subsidiary banks as well as general economic conditions; however, management is not presently aware of any reason dividend payments should not continue.

Dividends paid by the subsidiary banks are subject to restrictions by banking regulations. The most restrictive provision requires approval by the regulatory agency if dividends declared in any year exceed the year's net income, as defined, plus the retained net profits of the two preceding years. During 1999 the net retained profits available for distribution to South Branch as dividends without regulatory approval are approximately $730,000, plus net income for the interim periods through the date of declaration.

PENDING ACQUISITION, NEW SUBSIDIARY AND SUBSEQUENT EVENT

On December 23, 1998, the Company's subsidiary bank, CSB entered into an agreement to purchase three branch banking facilities located in Greenbrier County, West Virginia. The transaction is expected to be completed in April 1999, subject to approval by the appropriate regulatory authorities, and will include the branches' facilities and associated loan and deposit accounts. The offices will be operated as branches of CSB. Total deposits of the branches approximated $46.5 million and total loans approximated $11 million as of December 31, 1998. Under the terms of the purchase agreement, CSB will assume the deposits and acquire the loans of the branch offices. The total consideration to be paid is anticipated to be approximately $3.4 million and will be finally determined at closing based upon the total deposits assumed plus the seller's net book value of the branch offices and equipment.

On January 25, 1999, the Company received preliminary approval from the Office of the Comptroller of the Currency to begin organizing a new subsidiary bank, Shenandoah Valley National Bank, to be located in Winchester, Virginia. This newly chartered institution will be initially capitalized with $4,000,000, to be funded by a special dividend in the amount of $3,000,000 from the Company's subsidiary bank, SBVNB, and from a $1,000,000 term loan from an unaffiliated bank. Shenandoah Valley National Bank is expected to open in May 1999 pending final regulatory approvals.

On March 22, 1999, the Company entered into a letter of intent ("Letter") to affiliate with Potomac Valley Bank ("Potomac") in Petersburg, West Virginia. Under the terms of the Letter, South Branch and Potomac propose a merger whereby the shareholders of Potomac would exchange all of their outstanding shares of common stock for shares of South Branch common stock at a book-for-book exchange based on the respective book values of South Branch and Potomac as of the closing date. At December 31, 1998, the exchange ratio would have been 3.2143 shares of South Branch common stock for each share of Potomac's 90,000 outstanding shares of common stock. The terms of the Letter also include, among others, that the merger is subject to negotiation of a definitive merger agreement, South Branch changing its name to a name mutually agreeable to both parties, and approval of the transaction by all applicable regulatory authorities and the shareholders of South Branch and Potomac. It is expected that the transaction will be accounted for using the pooling of interests method of accounting. As of December 31, 1998, Potomac's assets, loans, deposits and shareholders' equity totaled $94,297,000, $50,393,000, $81,968,000 and $11,813,000, respectively.

Management does not anticipate that the above transactions will have any significant adverse impact on the Company's financial position, results of operations, liquidity or capital resources.

YEAR 2000

The Year 2000 Issue is the result of many existing computer programs and other date dependent electronic devices using only the last two digits, as opposed to four digits, to indicate the year. Such computer systems and devices may be unable to recognize a year that begins with 20XX instead of 19XX. If not corrected, the computer programs and devices could cause systems to fail or other computer errors, leading to possible disruptions in operations or creation of erroneous results. South Branch recognizes the significant potential risk associated with the Year 2000 Issue and, in a Company-wide effort, is taking steps to ensure that its internal systems are secure from such failure.

The Company's Year 2000 Plan ("Plan") addresses all its systems, software, hardware, and infrastructure components. The Plan identifies and addresses "Mission Critical" and "Non-mission Critical" components for Information Technology ("IT") systems and Non-information Technology ("Non-IT") systems. IT includes, for example, systems that service loan and deposit customers. Non-IT systems include security systems, elevators, utilities and voice/data communications. An application, system, or process is deemed "Mission Critical" if it is vital to the successful continuance of a core business activity.

South Branch's Plan follows a five phase approach recommended by bank regulatory authorities. These phases are: Awareness, Assessment, Renovation, Testing/Validation, and Implementation. During the Awareness Phase, management gathered information and appointed a project steering committee to coordinate the Company's Year 2000 efforts. In the Assessment Phase, South Branch identified its Mission Critical IT and Non-IT systems and performed an inventory of all systems, software, hardware, equipment and components that potentially could be affected by the Year 2000 issue. The Renovation Phase involves implementing program changes and new components, where applicable, to accommodate identified Year 2000 issues. In the Testing/Validation Phase, the Company is testing renovated applications and components to ensure they are Year 2000 compliant. During the Implementation Phase, applications, systems and other components are fine-tuned and final programs and components are placed into operation.

South Branch's estimated progress as of December 31, 1998 towards meeting the Plan's goals for both IT and Non-IT systems by phase are as follows:

Phase	Estimated Percent Complete	Estimated Completion Date
Mission Critical		
Awareness	100%	06/30/1998
Assessment	100%	09/30/1998
Renovation	95%	06/30/1999
Testing/Validation	95%	06/30/1999
Implementation	90%	06/30/1999
Non-mission Critical		
Awareness	100%	06/30/1998
Assessment	100%	09/30/1998
Renovation	90%	06/30/1999
Testing/Validation	90%	06/30/1999
Implementation	90%	06/30/1999

South Branch depends on various third-party vendors, suppliers, and service providers, and will be dependent on their continued service in order to avoid business interruptions. Any interruption in a third party's ability to provide goods and services, such as issues with telecommunication links and providers of electricity, could interrupt South Branch's ability to meet its customer's needs. South Branch has identified several third-party relationships considered Mission Critical, and is presently working with each to test transactions and/or interfaces between its processors, obtain appropriate information from each party, or assess each party's readiness with regard to the Year 2000 Issue.

Identifiable costs for the Company's Year 2000 project during 1998 approximated $131,000, of which $116,000 were capital expenditures for the replacement of computers and other date dependent electronic devices. The cost to complete the Plan in 1999 is not expected to exceed $50,000.

Major business risks associated with the Year 2000 problem include, but are not limited to, infrastructure failures, disruptions to the economy in general, excessive cash withdrawal activity, closure of government offices and clearing houses, and increased problem loans and credit losses in the event that borrowers fail to properly respond to the problem. These risks, along with the unlikely risk of South Branch failing to adequately complete the remaining phases of its Plan and the resulting possible inability to properly process business transactions expose the Company to loss of revenues, litigation, and asset quality deterioration.

The Year 2000 problem is unique in that it has never previously occurred; thus, it is not possible to completely foresee or quantify the overall or any specific financial or operational impacts to the Company or to third parties which provide Mission Critical services to the Company. South Branch is in the process of developing Year 2000 contingency plans in the event that Mission Critical third-party vendors or other third parties fail to adequately address Year 2000 issues. Such plans principally will involve internal remediation or identifying alternative vendors.

Item 7. Financial Statements

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
South Branch Valley Bancorp, Inc.
Moorefield, West Virginia

We have audited the accompanying consolidated balance sheets of South Branch Valley Bancorp, Inc. and subsidiaries as of December 31, 1998 and 1997, and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of South Branch Valley Bancorp, Inc. and subsidiaries as of December 31, 1998 and 1997, and the results of their operations and cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

ARNETT & FOSTER, P.L.L.C.

Charleston, West Virginia
February 11, 1999, except for Note 15
as to which the date is March 22, 1999

SOUTH BRANCH VALLEY BANCORP, INC., AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
December 31, 1998 and 1997

	1998	1997
ASSETS		
Cash and due from banks	$ 4,239,721	$ 3,945,099
Interest bearing deposits with other banks	770,000	1,256,000
Federal funds sold	4,842,745	5,806,717
Securities available for sale	31,409,924	27,547,094
Investment in affiliate	-	5,273,481
Loans, less allowance for loan losses of $1,371,886 and $895,281, respectively	142,770,127	92,572,652
Bank premises and equipment, net	5,170,858	3,071,064
Accrued interest receivable	1,059,990	864,083
Other assets	2,735,672	311,435
Total assets	$ 192,999,037	$ 140,647,625
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits		
Non interest bearing	$ 11,455,674	$ 9,693,915
Interest bearing	134,917,518	97,290,882
Total deposits	146,373,192	106,984,797
Short-term borrowings	4,644,143	7,145,010
Long-term borrowings	16,468,875	10,395,848
Other liabilities	1,367,698	1,061,418
Total liabilities	168,853,908	125,587,073
Commitments and Contingencies		
Shareholders' Equity		
Common stock, $2.50 par value, authorized 1998 - 2,000,000 shares, 1997 - 600,000 shares; issued 1998 - 600,407 shares, 1997 - 416,942 shares	1,501,018	1,042,355
Capital surplus	9,611,774	2,089,709
Retained earnings	13,103,264	11,898,420
Less cost of shares acquired for the treasury 1998-9,115 shares; 1997-4,115 shares	(384,724)	(166,970)
Accumulated other comprehensive income	313,797	197,038
Total shareholders' equity	24,145,129	15,060,552
Total liabilities and shareholders' equity	$192,999,037	$140,647,625

See Notes to Consolidated Financial Statements

SOUTH BRANCH VALLEY BANCORP, INC., AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
For The Years Ended December 31, 1998, 1997 and 1996

	1998	1997	1996
Interest income:			
Interest and fees on loans	$11,437,432	$8,558,144	$7,551,735
Interest and dividends on securities			
Taxable	1,813,205	1,540,530	1,711,158
Tax-exempt	320,769	314,596	254,988
Interest on interest bearing deposits with other banks	71,624	96,549	125,604
Interest on Federal funds sold	236,157	79,971	48,811
Total interest income	13,879,187	10,589,790	9,692,296
Interest expense:			
Interest on deposits	6,092,732	4,606,578	4,590,018
Interest on short-term borrowings	231,544	256,554	68,676
Interest on long-term borrowings	718,634	543,566	105,668
Total interest expense	7,042,910	5,406,698	4,764,362
Net interest income	6,836,277	5,183,092	4,927,934
Provision for loan losses	270,000	155,000	95,000
Net interest income after provision For loan losses	6,566,277	5,028,092	4,832,934
Other income:			
Insurance commissions	83,087	90,680	110,982
Trust services income	3,764	3,861	5,853
Service fees	430,840	280,442	232,845
Securities gains	8,160	9,789	29,999
Gain on sales of assets	17,751	89,919	7,202
Other	65,486	49,828	69,705
Total other income	609,088	524,519	456,586
Other expenses:			
Salaries and employee benefits	2,214,419	1,772,344	1,727,839
Net occupancy expense	300,369	196,005	189,285
Equipment rentals, depreciation and maintenance	388,860	289,223	222,543
Other	1,571,873	1,084,117	1,016,603
Total other expenses	4,475,521	3,341,689	3,156,270
Income before income tax expense	2,699,844	2,210,922	2,133,250
Income tax expense	966,550	691,265	643,213
Net income	$1,733,294	1,519,657	1,490,037
Basic earnings per common share	$ 3.16	$ 3.83	$ 3.94
Average common shares outstanding	548,331	397,032	378,510

See Notes to Consolidated Financial Statements

SOUTH BRANCH VALLEY BANCORP, INC., AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
For the Years Ended December 31, 1998, 1997 and 1996

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Compre-hensive Income	Total Share-holders' Equity
Balance, December 31, 1995	$ 956,562	$685,534	$9,512,884	$(166,970)	$340,650	$11,328,660
Comprehensive income:						
Net income	-	-	1,490,037	-	-	1,490,037
Other comprehensive income, net of tax:						
Net unrealized (loss) on securities of $(205,002), net of reclassification adjustment for gains included in net income of $18,449	-	-	-	-	(223,451)	(223,451)
Total comprehensive income	-	-	-	-	-	1,266,586
Cash dividends declared on common stock ($.77 per share)	-	-	(291,453)	-	-	(291,453)
Balance, December 31, 1996	956,562	685,534	10,711,468	(166,970)	117,199	12,303,793
Comprehensive income:						
Net income	-	-	1,519,657	-	-	1,519,657
Other comprehensive income, net of tax:						
Net unrealized gain on securities of $85,859, net of reclassification adjustment for gains included in net income of $6,020	-	-	-	-	79,839	79,839
Total comprehensive income	-	-	-	-	-	1,599,496
Net proceeds from issuance of 34,317 shares of common stock at $43.50 per share	85,793	1,404,175	-	-	-	1,489,968
Cash dividends declared on common stock ($.84 per share)	-	-	(332,705)	-	-	(332,705)
Balance, December 31, 1997	1,042,355	2,089,709	11,898,420	(166,970)	197,038	15,060,552

(Continued)

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY - Continued
For the Years Ended December 31, 1998, 1997 and 1996

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Compre-hensive Income	Total Share-holders' Equity
Comprehensive income:						
Net income	-	-	1,733,294	-	-	1,733,294
Other comprehensive income, net of tax:						
Net unrealized gain on securities of $121,777, net of reclassification adjustment for gains included in net income of $5,018	-	-	-	-	116,759	116,759
Total comprehensive income	-	-	-	-	-	1,850,053
Issuance of 183,465 shares of of common stock at $43.50 per share as consideration for the acquisition of Capital State Bank, Inc.	458,663	7,522,065	-	-	-	7,980,728
Cost of 5,000 shares of common stock acquired for the treasury	-	-	-	(217,754)	-	(217,754)
Cash dividends declared on common stock ($.89 per share)	-	-	(528,450)	-	-	(528,450)
Balance, December 31, 1998	$1,501,018	$9,611,774	$ 13,103,264	$ (384,724)	$ 313,797	$ 24,145,129

See Notes to Consolidated Financial Statements

SOUTH BRANCH VALLEY BANCORP, INC., AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 1998, 1997 and 1996

	1998	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 1,733,294	$ 1,519,657	$ 1,490,037
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation	330,091	235,488	212,383
Provision for loan losses	270,000	155,000	95,000
Deferred income tax (benefit) expense	17,288	47,839	(35,110)
Security (gains) losses	(8,160)	(9,789)	(29,999)
(Gain) on disposal of Bank premises and equipment	(9,709)	(91,507)	(23,176)
(Gain) loss on sale of other assets	(8,043)	1,588	(7,202)
Amortization of securities premium,s (accretion of discounts), net	(11,089)	10,069	50,141
Amortization of goodwill and purchase accounting adjustments, net	98,460	-	-
(Increase) decrease in accrued interest receivable	(3,027)	64,559	55,199
(Increase) decrease in other assets	334,993	574,396	(455,720)
Increase (decrease) in other liabilities	(264,044)	(12,752)	167,700
Net cash provided by operating activities	2,480,054	2,494,548	1,519,253
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from maturities of interest bearing deposits with other banks	486,000	297,000	581,919
Proceeds from maturities and calls of securities available for sale	10,390,000	6,748,200	3,950,000
Proceeds from sales of securities available for sale	613,160	1,539,666	6,735,258
Principal payments received on securities available for sale	3,053,020	1,417,948	768,591
Purchases of securities available for sale	(7,236,227)	(7,771,371)	(9,708,744)
Purchase of common stock of affiliate	(90,465)	(5,273,481)	-
(Increase) decrease in Federal funds sold, net	7,180,972	(5,082,983)	1,438,011
Loans made to customers, net	(26,083,150)	(10,387,784)	(11,950,307)
Purchases of Bank premises and equipment	(934,885)	(238,333)	(223,759)
Proceeds from disposal of Bank premises and equipment	10,693	145,180	93,011
Proceeds from sales of other assets	84,350	44,500	22,000
Net cash and due from banks acquired in acquisition of Capital State Bank, Inc.	985,617	-	-
Net cash (used in) investing activities	(11,540,915)	(18,561,458)	(8,294,020)

(Continued)

CONSOLIDATED STATEMENTS OF CASH FLOWS - Continued
For the Years Ended December 31, 1998, 1997 and 1996

	1998	1997	1996
CASH FLOWS FROM FINANCING ACTIVITIES			
Net increase (decrease) in demand deposit,			
NOW and savings accounts	2,120,609	(100,161)	(1,437,576)
Net increase (decrease) in time deposits	4,408,918	6,143,546	2,332,652
Net increase (decrease) in short-term borrowings	(2,500,867)	2,767,613	4,377,397
Proceeds from long-term borrowings	9,636,337	7,700,000	2,840,000
Repayment of long-term borrowings	(3,563,310)	(818,804)	(75,348)
Purchase of treasury stock	(217,754)	-	-
Dividends paid	(528,450)	(332,705)	(291,453)
Net proceeds from common stock sold	-	1,489,968	-
Net cash provided by financing activities	9,355,483	16,849,457	7,745,672
Increase (decrease) in cash and due from banks	294,622	782,547	970,905
Cash and due from banks:			
Beginning	3,945,099	3,162,552	2,191,647
Ending	$ 4,239,721	$ 3,945,099	$ 3,162,552
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Cash payments for:			
Interest	$ 7,042,088	$ 5,351,175	$ 4,742,367
Income taxes	$ 940,807	$ 604,871	$ 627,563
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES			
Other assets acquired in settlement of loans	$ 108,020	$ 74,337	$ 39,500
Acquisition of Capital State Bank, Inc.:			
Prior acquisition of 40% of the outstanding common shares purchased for cash	$5,363,946	$ -	$ -
Acquisition of 60% of the outstanding common shares in exchange for 183,465 shares of Company common stock	7,980,728	-	-
	$13,344,674	$ -	$ -
Fair value of assets acquired (principally loans and securities)	$46,720,306	$ -	$ -
Deposits and other liabilities assumed	(33,375,632)	-	-
	$13,344,674	$ -	$ -

See Notes to Consolidated Financial Statements

SOUTH BRANCH VALLEY BANCORP, INC., AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

NATURE OF BUSINESS: South Branch Valley Bancorp, Inc. ("Company") is a bank holding company with operations in Hardy, Grant, Pendleton and Kanawha Counties of West Virginia. Through its two wholly owned bank subsidiaries, South Branch Valley National Bank and Capital State Bank, Inc., the Company provides retail and commercial loans, and deposit and trust services principally to individuals and small businesses.

BASIS OF FINANCIAL STATEMENT PRESENTATION: The accounting and reporting policies of South Branch Valley Bancorp, Inc., and its subsidiaries conform to generally accepted accounting principles and to general practices within the banking industry.

USE OF ESTIMATES: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

PRINCIPLES OF CONSOLIDATION: The accompanying consolidated financial statements include the accounts of South Branch Valley Bancorp, Inc., and its subsidiaries, South Branch Valley National Bank and Capital State Bank, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

PRESENTATION OF CASH FLOWS: For purposes of reporting cash flows, cash and due from banks includes cash on hand and amounts due from banks (including cash items in process of clearing). Cash flows from demand deposits, NOW accounts, savings accounts and Federal funds purchased and sold are reported net, since their original maturities are less than three months. Cash flows from loans and certificates of deposit and other time deposits are reported net.

SECURITIES: Debt and equity securities are classified as "held to maturity", "available for sale" or "trading" according to management's intent. The appropriate classification is determined at the time of purchase of each security and re-evaluated at each reporting date.

Securities held to maturity - There are no securities classified as "held to maturity" in the accompanying consolidated financial statements.

Securities available for sale - Securities not classified as "held to maturity" or as "trading" are classified as "available for sale." Securities classified as "available for sale" are those securities the Bank intends to hold for an indefinite period of time, but not necessarily to maturity. "Available for sale" securities are reported at estimated fair value net of unrealized gains or losses, which are adjusted for applicable income taxes, and reported as a separate component of shareholders' equity.

Trading securities - There are no securities classified as "trading" in the accompanying consolidated financial statements.

Realized gains and losses on sales of securities are recognized on the specific identification method. Amortization of premiums and accretion of discounts are computed using the interest method.

LOANS AND ALLOWANCE FOR LOAN LOSSES: Loans are stated at the amount of unpaid principal, reduced by unearned discount and an allowance for loan losses.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. The allowance is increased by provisions charged to operating expense and reduced by net charge-offs. The subsidiary banks make continuous credit reviews of the loan portfolio and consider current economic conditions, historical loan loss experience, review of specific problem loans and other factors in determining the adequacy of the allowance for loan losses. Loans are charged against the allowance for loan losses when management believes that collectibility is unlikely. While management uses the best information available to make its evaluation, future adjustments may be necessary if there are significant changes in conditions.

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due in accordance with the contractual terms of the specific loan agreement. Impaired loans, other than certain large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment, are required to be reported at the present value of expected future cash flows discounted using the loan's original effective interest rate or, alternatively, at the loan's observable market price, or at the fair value of the loan's collateral if the loan is collateral dependent. The method selected to measure impairment is made on a loan-by-loan basis, unless foreclosure is deemed to be probable, in which case the fair value of the collateral method is used.

Generally, after management's evaluation, loans are placed on non-accrual status when principal or interest is greater than 90 days past due based upon the loan's contractual terms. Interest is accrued daily on impaired loans unless the loan is placed on non-accrual status. Impaired loans are placed on non-accrual status when the payments of principal and interest are in default for a period of 90 days, unless the loan is both well-secured and in the process of collection. Interest on non-accrual loans is recognized primarily using the cost-recovery method.

Unearned interest on discounted loans is amortized to income over the life of the loans, using methods which approximate the interest method. For all other loans, interest is accrued daily on the outstanding balances.

Certain loan fees and direct loan costs are recognized as income or expense when incurred. Whereas, generally accepted accounting principles require that such fees and costs be deferred and amortized as adjustments of the related loan's yield over the contractual life of the loan. The Company's method of recognition of loan fees and direct loan costs produces results which are not materially different from those that would be recognized had Statement of Financial Accounting Standards Board No. 91 been adopted.

BANK PREMISES AND EQUIPMENT: Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed primarily by the straight-line method for bank premises and equipment over the estimated useful lives of the assets. The estimated useful lives employed are on average 30 years for premises and 3 to 10 years for furniture and equipment. Repairs and maintenance expenditures are charged to operating expenses as incurred. Major improvements and additions to premises and equipment, including construction period interest costs, are capitalized. No interest was capitalized during any period presented in the accompanying financial statements.

OTHER REAL ESTATE: Other real estate consists primarily of real estate held for resale which was acquired through foreclosure on loans secured by such real estate. At the time of acquisition, these properties are recorded at fair value with any write own being charged to the allowance for loan losses. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of carrying amount or fair value, less cost to sell.

Expenses incurred in connection with operating these properties are generally insignificant and are charged to operating expenses. Gains and losses on the sales of these properties are credited or charged to operating income in the year of the transactions.

Other real estate acquired through foreclosure with carrying values of $84,655 and $57,465, at December 31, 1998 and 1997, respectively, is included in other assets in the accompanying consolidated balance sheets.

INCOME TAXES: The consolidated provision for income taxes includes Federal and state income taxes and is based on pretax net income reported in the consolidated financial statements, adjusted for transactions that may never enter into the computation of income taxes payable. Deferred tax assets and liabilities are determined based on the differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. Valuation allowances are established when deemed necessary to reduce deferred tax assets to the amount expected to be realized.

BASIC EARNINGS PER SHARE: Basic earnings per common share are computed based upon the weighted average shares outstanding. The weighted average number of shares outstanding was 548,331, 397,032 and 378,510 for the years ended December 31, 1998, 1997 and 1996, respectively. For the year ended December 31, 1997, the Company adopted Financial Accounting Standards Board Statement No. 128, Earnings Per Share.

EMPLOYEE BENEFITS: The Company has a profit-sharing and thrift plan and an employee stock ownership plan (ESOP) which covers substantially all employees. The amount of the contributions to the plans are at the discretion of the Company's Board of Directors.

TRUST SERVICES: Assets held in an agency or fiduciary capacity are not assets of the Company and are not included in the accompanying consolidated balance sheets. Trust services income is recognized on the cash basis in accordance with customary banking practice. Reporting such income on a cash basis rather than the accrual basis does not have a material effect on net income.

COMPREHENSIVE INCOME: During 1998, the Company adopted Financial Accounting Standards Board Statement No. 130, Reporting Comprehensive Income. This Statement establishes standards for reporting the components of comprehensive income and requires that all items that are required to be recognized under accounting standards as components of comprehensive income be included in a financial statement that is displayed with the same prominence as other financial statements. Comprehensive income includes net income as well as certain items that are reported directly within a separate component of shareholders' equity and bypass net income.

EMERGING ACCOUNTING STANDARDS: In June 1998, the Financial Accounting Standards Board issued Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, which is required to be adopted in years beginning after June 15, 1999. The Company expects to adopt the new Statement effective December 31, 2000. The Statement will require the Company to recognize all derivatives on the consolidated balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through income.

If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings or recognized in other comprehensive income until the hedged items are recognized in earnings. The ineffective portion of a derivative's change in fair value will be immediately recognized in earnings. Management does not anticipate that the adoption of the new Statement will have a significant impact on the Company's earnings or financial position.

RECLASSIFICATIONS: Certain accounts in the consolidated financial statements for 1997 and 1996, as previously presented, have been reclassified to conform to current year classifications.

NOTE 2. ACQUISITION OF CAPITAL STATE BANK, INC.

During the first half of 1997, the Company purchased approximately 40% of the outstanding common shares of Capital State Bank, Inc ("Capital State"). To facilitate the funding of this investment, the Company issued and sold 34,317 shares of its common stock at $43.50 per share to seven directors of the Company in a limited stock offering. Additionally, the Company obtained two long-term borrowings from two unaffiliated financial institutions totaling $3,500,000. The Company's investment in Capital State as of December 31, 1997 totaled $5,273,481, and is reflected as investment in affiliate in the 1997 accompanying consolidated balance sheet.

On August 6, 1997, the Company entered into an Agreement and Plan of Merger with Capital State to acquire the remaining 60% of its outstanding common shares. The Agreement, as amended on December 16, 1997, provided for the shareholders of Capital State to receive one (1) share of the Company's common stock in exchange for each 3.95 shares of Capital State stock owned. To facilitate this transaction, the Company issued a total of 183,465 shares of its common stock. On March 24, 1998 and March 25, 1998, the shareholders of Capital State and the Company respectively, approved the transaction and, it was consummated at the close of business on March 31, 1998. This acquisition was accounted for using the purchase method of accounting, and accordingly, the assets and liabilities and results of operations of Capital State are reflected in the Company's consolidated financial statements beginning April 1, 1998. The excess purchase price over the fair value of the net assets acquired as of the consummation date totaled $1,979,430, which is included in other assets in the accompanying consolidated balance sheet as of December 31, 1998. This goodwill is being amortized over a period of 15 years using the straight line method.

The following presents certain pro forma condensed consolidated financial information of the Company, using the purchase method of accounting, after giving effect to the merger as if it had been consummated at the beginning of the periods presented (in thousands, except per share data).

	For the Year Ended					
	December 31, 1998		December 31, 1997		December 31, 1996	
	As Reported	Pro Forma	As Reported	Pro Forma	As Reported	Pro Forma
Total interest income	$13,879	$14,614	$10,590	$13,137	$9,692	$11,125
Total interest expense	7,043	7,431	5,407	6,568	4,764	5,239
Net interest income	6,836	7,183	5,183	6,569	4,928	5,886
Net income	1,733	1,746	1,520	1,304	1,490	1,113
Basic earnings per share	$ 3.16	$ 2.94	$ 3.83	$ 2.25	$ 3.94	$1.98

This pro forma information has been included for comparative purposes only and may not be indicative of the combined results of operations that actually would have occurred had the transaction been consummated at the beginning of the periods presented, or which will be attained in the future.

NOTE 3. CASH CONCENTRATION

At December 31, 1998 and 1997, the Company had concentrations totaling $4,626,123 and $8,514,792, respectively, with unaffiliated financial institutions consisting of due from bank account balances and Federal funds sold. Deposits with correspondent banks are generally unsecured and have limited insurance under current banking insurance regulations.

NOTE 4. SECURITIES

The amortized cost, unrealized gains and losses, and estimated fair values of securities at December 31, 1998 and 1997, are summarized as follows:

	1998			
	Amortized	Unrealized		Estimated
	Cost	Gains	Losses	Fair Value
Available for Sale				
Taxable:				
U. S. Treasury securities	$2,990,294	$ 68,354	$ -	$3,058,648
U. S. Government agencies and corporations	12,698,092	82,796	11,404	12,769,484
Small Business Administration guaranteed loan participation certificates	973,127	21,119	-	994,246
Mortgage-backed securities - U. S. Government agencies and corporations	6,334,380	86,483	-	6,420,863
Corporate debt securities	249,724	1,214	-	250,938
Federal Reserve Bank stock	44,300	-	-	44,300
Federal Home Loan Bank stock	1,052,300	-	-	1,052,300
Other equity securities	306,625	-	-	306,625
Total taxable	24,648,842	259,966	11,404	24,897,404
Tax-exempt:				
State and political subdivisions	6,246,745	268,525	6,850	6,508,420
Federal Reserve Bank stock	4,100	-	-	4,100
Total tax-exempt	6,250,845	268,525	6,850	6,512,520
Total	$30,899,687	$528,491	$ 18,254	$31,409,924

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1997

	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Available for Sale				
Taxable:				
U. S. Treasury securities	$2,988,064	$46,546	$ -	$3,034,610
U. S. Government agencies and corporations	9,523,135	71,935	8,850	9,586,220
Small Business Administration guaranteed loan participation certificates	1,470,915	16,522	-	1,487,437
Mortgage-backed securities - U. S. Government agencies and corporations	6,650,070	21,182	20,328	6,650,924
Corporate debt securities	249,082	3,296	-	252,378
Federal Reserve Bank stock	44,300	-	-	44,300
Federal Home Loan Bank stock	722,400	-	-	722,400
Other equity securities	6,625	-	-	6,625
Total taxable	21,654,591	159,481	29,178	21,784,894
Tax-exempt:				
State and political subdivisions	5,568,016	190,084	-	5,758,100
Federal Reserve Bank stock	4,100	-	-	4,100
Total tax-exempt	5,572,116	190,084	-	5,762,200
Total	$27,226,707	$349,565	$29,178	$27,547,094

Federal Reserve Bank stock and Federal Home Loan Bank stock are equity securities which are included in securities available for sale in the accompanying consolidated financial statements. Such securities are carried at cost, since they may only be sold back to the respective Federal Reserve Bank or Federal Home Loan Bank or another member at par value.

Mortgage-backed obligations of U.S. Government agencies and corporations and Small Business Administration guaranteed loan participation certificates are included in securities at December 31, 1998 and 1997. These obligations, having contractual maturities ranging from 1 to 20 years, are reflected in the following maturity distribution schedules based on their anticipated average life to maturity, which ranges from 1 to 5 years. Accordingly, discounts are accreted and premiums are amortized over the anticipated average life to maturity of the specific obligation.

The maturities, amortized cost and estimated fair values of securities at December 31, 1998, are summarized as follows:

	Available for Sale	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 6,970,026	$ 7,043,402
Due from one to five years	13,792,274	14,009,639
Due from five to ten years	6,556,501	6,661,720
Due after ten years	2,173,561	2,287,838
Equity securities	1,407,325	1,407,325
Total	$30,899,687	$31,409,924

The proceeds from sales, calls and maturities of securities, including principal payments received on mortgage-backed obligations and the related gross gains and losses realized are as follows:

Years Ended December 31,	Proceeds from Sales	Proceeds from Calls and Maturities	Proceeds from Principal Payments	Gross Realized Gains	Gross Realized Losses
1998					
Securities available for sale	$ 613,160	$10,390,000	$3,053,020	$8,160	$ -
1997					
Securities available for sale	$1,539,666	$ 6,748,200	$1,417,948	$9,789	$ -
1996					
Securities available for sale	$6,735,258	$ 3,950,000	$ 768,591	$45,824	$15,825

At December 31, 1998 and 1997, securities with amortized costs of $17,676,849 and $17,149,748, respectively, with estimated fair values of $17,973,561 and $17,313,961, respectively, were pledged to secure public deposits, and for other purposes required or permitted by law.

NOTE 5. LOANS

Loans are summarized as follows:

	1998	1997
Commercial, financial and agricultural	$41,956,586	$30,325,145
Real estate - construction	1,801,317	144,207
Real estate - mortgage	73,885,892	42,640,294
Installment	26,579,782	20,587,084
Other	409,382	468,980
Total loans	144,632,959	94,165,710
Less unearned income	490,946	697,777
Total loans net of unearned income	144,142,013	93,467,933
Less allowance for loan losses	1,371,886	895,281
Loans, net	$142,770,127	$92,572,652

Included in the net balance of loans are non-accrual loans amounting to $297,291 and $141,735 at December 31, 1998 and 1997, respectively. If interest on non-accrual loans had been accrued, such income would have approximated $15,487, $14,200 and $30,978 for the years ended December 31, 1998, 1997 and 1996, respectively.

The following presents loan maturities at December 31, 1998:

	Within 1 Year	After 1 but Within 5 Years	After 5 Years
Commercial, financial and agricultural	$8,958,628	$10,957,213	$22,040,745
Real estate - construction	1,723,368	-	77,949
Real estate - mortgage	2,476,797	9,048,985	62,360,110
Installment loans	3,347,660	19,629,580	3,602,542
Other	374,915	34,467	-
Total	$16,881,368	$39,670,245	$88,081,346

Loans due after one year with:	
Variable rates	$ 41,111,653
Fixed rates	86,639,938
	$127,751,591

The Company has made, and may be expected to make in the future, commercial and mortgage loans that have adjustable rates. Such loan rates are generally indexed to the Wall Street prime interest rate or to other common indices. At December 31, 1998, the Company's commercial loan portfolio contained adjustable rate loans of approximately $20,375,879. The interest rates on such loans ranged from 7.0% to 11.5%, and provided for future interest rate changes at set intervals, ranging from one to sixty months.

Likewise, the Company's mortgage portfolio contained adjustable rate loans of approximately $26,701,170 at December 31, 1998. The interest rates on such loans ranged from 6.3% to 14.5%, and provided for future interest rate changes at set intervals, ranging from monthly to fifteen years.

CONCENTRATIONS OF CREDIT RISK: The Company grants commercial, residential and consumer loans to customers primarily located in the Eastern Panhandle and South Central counties of West Virginia. Although the Company strives to maintain a diverse loan portfolio, exposure to credit losses can be adversely impacted by downturns in local economic and employment conditions. Major employment within the Company's market area is diverse, but primarily includes the poultry, government, health care, education, coal production and various professional, financial and related service industries.

The Company evaluates the credit worthiness of each of its customers on a case-by-case basis and the amount of collateral it obtains is based upon management's credit evaluation.

LOANS TO RELATED PARTIES: The subsidiary banks have had, and may be expected to have in the future, banking transactions in the ordinary course of business with directors, principal officers, their immediate families and affiliated companies in which they are principal stockholders (commonly referred to as related parties), all of which have been, in the opinion of management, on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others.

The following presents the activity with respect to related party loans aggregating $60,000 or more to any one related party (other changes represent additions to and changes in director and executive officer status):

	1998	1997
Balance, beginning	$ 3,913,943	$ 4,318,097
Additions	2,185,541	1,651,121
Amounts collected	(1,373,239)	(1,483,575)
Other changes, net	784,133	(571,700)
Balance, ending	$ 5,510,378	$ 3,913,943

NOTE 6. ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses for the years ended December 31, 1998, 1997 and 1996, is as follows:

	1998	1997	1996
Balance, beginning of year	$ 895,281	$ 858,423	$ 859,681
Losses:			
Commercial, financial and agricultural	4,063	-	10,194
Real estate - mortgage	-	25,536	12,778
Installment	124,103	166,059	93,826
Other	24,638	8,444	9,951
Total	152,804	200,039	126,749
Recoveries:			
Commercial, financial and agricultural	2,830	27,050	5,658
Real estate - mortgage	21,969	13,675	1,885
Installment	60,797	39,936	20,525
Other	2,011	1,236	2,423
Total	87,607	81,897	30,491
Net losses	65,197	118,142	96,258
Allowance of purchased subsidiary	271,802	-	-
Provision for loan losses	270,000	155,000	95,000
Balance, end of year	$1,371,886	$895,281	$858,423

The Company's total recorded investment in impaired loans at December 31, 1998 and 1997, approximated $354,907 and $125,114, respectively, for which the related allowance for loan losses determined in accordance with generally accepted accounting principles approximated $51,000 and $77,500, respectively. The Company's average investment in such loans approximated $368,326 and $125,114 for the years ended December 31, 1998 and 1997, respectively. All impaired loans at December 31, 1998 and 1997, were collateral dependent, and accordingly, the fair value of the loan's collateral was used to measure the impairment of each loan.

For purposes of evaluating impairment, the Company considers groups of smaller-balance, homogeneous loans to include: mortgage loans secured by residential property, other than those which significantly exceed the Company's typical residential mortgage loan amount (currently those in excess of $100,000); small balance commercial loans (currently those less than $50,000); and installment loans to individuals, exclusive of those loans in excess of $50,000.

For the years ended December 31, 1998 and 1997, the Company recognized approximately $29,760 and $12,272, respectively, in interest income on impaired loans. Using a cash-basis method of accounting, the Company would have recognized approximately the same amount of interest income on such loans.

NOTE 7. BANK PREMISES AND EQUIPMENT

The major categories of Bank premises and equipment and accumulated depreciation at December 31, 1998 and 1997, are summarized as follows:

	1998	1997
Land	$ 1,174,679	$ 429,973
Buildings and improvements	3,928,162	2,681,707
Furniture and equipment	2,327,419	1,675,258
	7,430,260	4,786,938
Less accumulated depreciation	2,259,402	1,715,874
Bank premises and equipment, net	$ 5,170,858	$3,071,064

Depreciation expense for the years ended December 31, 1998, 1997 and 1996 totaled $330,091, $235,488 and $212,383, respectively.

NOTE 8. DEPOSITS

The following is a summary of interest bearing deposits by type as of December 31, 1998 and 1997:

	1998	1997
Demand deposits, interest bearing	$ 27,510,717	$17,468,844
Savings deposits	14,748,928	14,890,934
Certificates of deposit	83,319,247	56,902,451
Individual retirement accounts	9,338,626	8,028,653
Total	$134,917,518	$97,290,882

Time certificates of deposit and IRA's in denominations of $100,000 or more totaled $22,262,990 and $10,726,460 at December 31, 1998 and 1997, respectively. Interest paid on time certificates of deposit and Individual Retirement Accounts in denominations of $100,000 or more was $1,103,306, $565,000 and $501,754 for the years ended December 31, 1998, 1997 and 1996, respectively.

The following is a summary of the maturity distribution of certificates of deposit and IRA's in denominations of $100,000 or more as of December 31, 1998:

	Amount	Percent
Three months or less	$ 2,719,367	12.2%
Three through six months	5,171,279	23.2%
Six through twelve months	7,982,333	35.9%
Over twelve months	6,390,011	28.7%
Total	$22,262,990	100.0%

A summary of the scheduled maturities for all time deposits as of December 31, 1998, follows:

1999	$61,542,656
2000	18,123,034
2001	5,925,183
2002	2,410,855
2003	3,692,763
Thereafter	963,382
	$92,657,873

At December 31, 1998, deposits of related parties including directors, executive officers, and their related interests of the Company approximated $7,880,000.

NOTE 9. OTHER BORROWINGS

Short-term borrowings: Federal funds purchased and securities sold under agreements to repurchase mature the next business day. The securities underlying the repurchase agreements are under the subsidiary banks' control and secure the total outstanding daily balances. Other borrowings consist of lines of credit from the Federal Home Loan Bank (FHLB) under its RepoPlus Program. The RepoPlus is limited to the subsidiary banks' outstanding maximum borrowing capacity of approximately $45,433,000 at December 31, 1998, less the current outstanding balance of any long-term FHLB borrowings, and is subject to annual renewal. Borrowings under this arrangement will be granted for terms of 1 to 364 days and will bear interest at a fixed rate set at the time of the funding request. The lines of credit are secured by a blanket lien on all unpledged and unencumbered assets of the subsidiary banks.

Additional details regarding short-term borrowings during the years ended December 31, 1998 and 1997, are presented below:

	1998		
	Federal Funds Purchased	Repurchase Agreements	Other Borrowings
Outstanding at year end	$ -	$3,944,143	$700,000
Average amount outstanding	82,164	4,981,296	307,219
Maximum amount outstanding at any month end	700,000	5,959,583	1,400,000
Weighted average interest rate	6.29%	4.20%	5.49%

	1997		
	Federal Funds Purchased	Repurchase Agreements	Other Borrowings
Outstanding at year end	$ -	$5,745,010	$1,400,000
Average amount outstanding	107,534	3,853,897	1,724,015
Maximum amount outstanding at any month end	-	5,745,010	2,400,000
Weighted average interest rate	5.33%	4.21%	5.14%

Long-term borrowing: On February 18, 1997 and March 14, 1997, the Company obtained two long-term borrowings from two separate, unaffiliated financial institutions in the amounts of $3,000,000 and $500,000 respectively, to fund a portion of its investment in an affiliate. Both of these borrowings were paid off in 1998.

The subsidiary banks also had long-term borrowings of $16,468,875 and $7,558,348 as of December 31, 1998 and 1997, respectively, which consisted of advances from the Federal Home Loan Bank of Pittsburgh to fund local mortgage loan growth. These borrowings bear both fixed and variable interest rates and mature in varying amounts through the year 2008. The average interest rate paid during 1998 and 1997 approximated 5.35% and 6.11%, respectively.

A summary of the maturities of all long-term borrowings for the next five years and thereafter is as follows:

Year Ending December 31,	Amount
1999	$1,026,364
2000	856,611
2001	378,079
2002	3,150,840
2003	2,424,974
Thereafter	8,632,007
	$16,468,875

NOTE 10. INCOME TAXES

The components of applicable income tax expense (benefit) for the years ended December 31, 1998, 1997 and 1996, are as follows:

	1998	1997	1996
Current			
Federal	$ 832,962	$563,735	$602,391
State	116,300	79,691	75,932
	949,262	643,426	678,323
Deferred			
Federal	19,359	39,640	(31,208)
State	(2,071)	8,199	(3,902)
	17,288	47,839	(35,110)
Total	$ 966,550	$691,265	$643,213

A reconciliation between the amount of reported income tax expense and the amount computed by multiplying the statutory income tax rates by book pretax income for the years ended December 31, 1998, 1997 and 1996 is as follows:

	1998		1997		1996	
	Amount	Percent	Amount	Percent	Amount	Percent
Computed tax at applicable statutory rate	$ 917,947	34	$751,713	34	$725,305	34
Increase (decrease) in taxes resulting from:						
Tax-exempt interest, net	(92,251)	(3)	(94,460)	(4)	(80,961)	(4)
State income taxes, net of Federal income tax benefit	75,391	3	58,007	3	47,540	2
Change in deferred tax valuation allowance	61,965	2	15,758	1	5,237	-
Nondeductible amortization of goodwill	33,415	1	-	-	-	-
Noncash charitable contribution	-	-	(41,573)	(2)	(59,704)	(3)
Other, net	(29,917)	(1)	1,820	-	5,796	1
Applicable income taxes	$ 966,550	36	$691,265	32	$643,213	30

Deferred income taxes reflect the impact of "temporary differences" between amounts of assets and liabilities for financial reporting purposes and such amounts as measured for tax purposes. Deferred tax assets and liabilities represent the future tax return consequences of temporary differences, which will either be taxable or deductible when the related assets and liabilities are recovered or settled. Valuation allowances are established when deemed necessary to reduce deferred tax assets to the amount expected to be realized.

The tax effects of temporary differences which give rise to the Company's deferred tax assets and liabilities as of December 31, 1998 and 1997, are as follows:

	1998	1997
Deferred tax assets		
Allowance for loan losses	$ 380,420	$226,964
Deferred compensation	80,803	62,137
Other deferred costs and accrued expenses	65,558	-
Deductible goodwill	29,235	9,482
Net operating loss carryforwards	90,589	-
Charitable contribution carryforward	1,226	-
	647,831	298,583
Less valuation allowance	(271,733)	(209,768)
	376,098	88,815
Deferred tax liabilities		
Depreciation	115,432	51,225
Net unrealized gain on securities	196,440	123,349
Accretion on tax-exempt securities	6,120	2,519
Purchase accounting adjustments	106,126	-
Deferred gain on disposal of premises and equipment	-	15,135
	424,118	192,228
Net deferred tax assets (liabilities)	$ (48,020)	$(103,413)

The income tax expense (benefit) on realized securities gains (losses) was $3,142, $3,769 and $11,550, for the years ended December 31, 1998, 1997 and 1996, respectively. The Company has available for tax purposes $194,818 and $249,674, respectively, in Federal and State net operating loss carryforwards to offset future taxable income of Capital State Bank, Inc. These carryforwards expire in varying amounts through 2011.

NOTE 11. EMPLOYEE BENEFITS

Profit-Sharing and Thrift Plan: The Company has a defined contribution profit-sharing and thrift plan with 401(k) provisions covering substantially all employees. Contributions to the Plan are at the discretion of the Board of Directors. Contributions made to the Plan and charged to expense were $61,859, $53,417, and $54,240 for the years ended December 31, 1998, 1997 and 1996, respectively.

EMPLOYEE STOCK OWNERSHIP PLAN: The Company has an Employee Stock Ownership Plan (ESOP) which enables eligible employees to acquire shares of the Company's common stock. The cost of the ESOP is borne by the Company through annual contributions to an Employee Stock Ownership Trust in amounts determined by the Board of Directors.

The expense recognized by the Company is based on cash contributed or committed to be contributed by the Company to the ESOP during the year. Contributions to the ESOP for the years ended December 31, 1998, 1997 and 1996 were $54,559, $51,047 and $48,250, respectively. Dividends made by the Company to the ESOP are reported as a reduction to retained earnings. The ESOP owns 11,560 shares of the Company's common stock, all of which were purchased at the prevailing market price and are considered outstanding for earnings per share computations.

The trustees of both the Profit-Sharing and Thrift Plan and ESOP are also members of the Company's Board of Directors.

INCENTIVE COMPENSATION PROGRAM: South Branch Valley National Bank has an incentive compensation program for its key employees. Bonuses are awarded to key employees based on a prescribed formula using the Bank's return on equity as a base. Under the terms of the incentive compensation program, bonuses charged to operations totaled $185,000, $141,000 and $137,000 for 1998, 1997 and 1996, respectively.

DIRECTORS DEFERRED COMPENSATION PLAN: South Branch Valley National Bank has established a non-qualified deferred compensation plan for directors who voluntarily elect to participate. Under that plan, a director, on or before December 31, of any year, may elect to defer payment of all retainer, meeting and committee fees earned during the calendar year following such election and, unless such election is subsequently terminated, all succeeding calendar years. Amounts deferred are periodically converted to units representing shares of the Company's stock which are to be periodically purchased by the plan at current market values when available on the open market.

In December 1998, the Directors of South Branch Valley National Bank voted in principle to amend and restate this plan by revoking all units of Company common stock previously assigned to participants and to invest all prior and future deferrals of fees in separate variable life insurance contracts. The Company expects to complete the amendment and restatement of this plan in 1999.

The liability for deferred directors' compensation at December 31, 1998 and 1997, approximated $211,250 and $162,450, respectively, which is included in other liabilities in the accompanying consolidated balance sheets.

STOCK OPTION PLAN: In April 1998, the Company's shareholders approved the 1998 Officer Stock Option Plan. Under the terms of the plan, the Company's Board of Directors or its designated committee may grant options for up to 120,000 shares of common stock to officers employed by the Company or its subsidiaries. Each option granted under the plan shall have a term of no more than 10 years and an exercise price no less than the fair market value of the Company's common stock as of the date of grant. Options granted under the plan vest according to a schedule designated at the grant date. The Company intends to account for grants under this plan in accordance with APB Opinion No. 25. As of December 31, 1998, no options had been granted under the plan.

In February 1999, the Company's Board of Directors voted to grant a total of 7,500 options to certain of its officers. These options have a term of 10 years, vest ratably over 5 years, and have an exercise price of $41.65.

NOTE 12. COMMITMENTS AND CONTINGENCIES

FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK: The Company is a party of certain financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. Such financial instruments consist solely of commitments to extend credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statement of financial position. The contract amounts of these instruments reflect the extent of involvement the Company has in this class of financial instruments. The Company's total contract amount of commitments to extend credit at December 31, 1998 and 1997, approximated $9,155,179 and $5,715,032, respectively.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract.

Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, equipment or real estate.

LITIGATION: The Company is involved in various legal actions arising in the ordinary course of business. In the opinion of counsel, the outcome of these matters will not have a significant adverse effect on the consolidated financial statements.

EMPLOYMENT AGREEMENTS: The Company has various employment agreements with its chief executive officer and certain other senior executive officers. These agreements contain change in control provisions that would entitle the officers to receive compensation in the event there is a change in control in the Company (as defined) and a termination of their employment without cause (as defined).

YEAR 2000 READINESS: The Year 2000 Issue ("Issue") relates to whether computer and other electronic systems will properly recognize date-sensitive information when the year changes from 1999 to 2000. Since the Company and its suppliers, customers, and service providers are heavily dependent on computer processing in the conduct of business, a plan was developed to study, test and remedy the Issue. As a result, a remediation plan and processes were developed and implemented and the Company made expenditures approximating $131,000 during 1998, of which $116,000 were capital expenditures for the replacement of computers and other date dependent electronic devices and processes. To complete the remediation plan, limited additional remediation will be completed in the first half of 1999, the cost of which is not expected to exceed $50,000.

Based on the actions taken and the processes implemented regarding remediation of the Issue, management feels that risks from potential Year 2000 business disruptions have been minimized to the extent possible. Management will continue to analyze and monitor all systems and processes over which it has control throughout 1999. Also, contingency plans have been developed to minimize risks of Year 2000 disruptions from sources outside of the Company's control.

NOTE 13. RESTRICTIONS ON CAPITAL AND DIVIDENDS

The primary source of funds for the dividends paid by South Branch Valley Bancorp, Inc. is dividends received from its subsidiary banks. Dividends paid by the subsidiary banks are subject to restrictions by banking regulations. The most restrictive provision requires approval by their regulatory agencies if dividends declared in any year exceed the year's net income, as defined, plus the net retained profits of the two preceding years. During 1999, the net retained profits available for distribution to South Branch Valley Bancorp, Inc. as dividends without regulatory approval are approximately $730,000 plus net retained income of the subsidiary banks for the interim periods through the date of declaration.

The Company and its subsidiaries are subject to various regulatory capital requirements administered by the banking regulatory agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and each of its subsidiaries must meet specific capital guidelines that involve quantitative measures of the Company's and its subsidiaries' assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Company and each of its subsidiaries' capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and each of its subsidiaries to maintain minimum amounts and ratios of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 1998, that the Company and each of its subsidiaries met all capital adequacy requirements to which they were subject.

The most recent notifications from the banking regulatory agencies categorized the Company and each of its subsidiaries as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Company and each of its subsidiaries must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table below.

The Company's and its subsidiaries', South Branch Valley National Bank's ("SBVNB") and Capital State Bank, Inc.'s ("CSB"), actual capital amounts and ratios are also presented in the following table (dollar amounts in thousands).

	Actual		Minimum Required Regulatory Capital		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 1998						
Total Capital (to risk weighted assets)						
Company	$23,309	18.4%	$10,126	8.0%	$12,658	10.0%
SBVNB	13,510	14.0%	7,721	8.0%	9,652	10.0%
CSB	8,976	30.5%	2,356	8.0%	2,945	10.0%
Tier I Capital (to risk weighted assets)						
Company	21,937	17.3%	5,063	4.0%	7,595	6.0%
SBVNB	12,468	12.9%	3,861	4.0%	5,791	6.0%
CSB	8,646	29.4%	1,178	4.0%	1,767	6.0%
Tier I Capital (to average assets)						
Company	21,937	11.5%	5,702	3.0%	9,504	5.0%
SBVNB	12,468	8.7%	4,289	3.0%	7,148	5.0%
CSB	8,646	17.7%	1,464	3.0%	2,441	5.0%
As of December 31, 1997						
Total Capital (to risk weighted assets)						
Company	$15,759	17.7%	$7,126	8.0%	$8,908	10.0%
SBVNB	12,779	14.4%	7,123	8.0%	8,904	10.0%
CSB	*	*	*	*	*	*
Tier I Capital (to risk weighted assets)						
Company	$14,864	16.7%	$3,563	4.0%	$5,345	6.0%
SBVNB	11,884	13.4%	3,562	4.0%	5,342	6.0%
CSB	*	*	*	*	*	*
Tier I Capital (to average assets)						
Company	14,864	11.3%	3,941	3.0%	6,569	5.0%
SBVNB	11,884	9.2%	3,897	3.0%	6,494	5.0%
CSB	*	*	*	*	*	*

* - No data presented relative to CSB for the year ended December 31, 1997, as this subsidiary was acquired by the Company in March 1998.

NOTE 14. PENDING ACQUISITION AND NEW SUBSIDIARY

On December 23, 1998, a subsidiary of the Company, Capital State Bank, Inc. entered into an agreement to purchase three branch banking facilities located in Greenbrier County, West Virginia. The transaction is expected to be completed in April 1999, subject to approval by the appropriate regulatory authorities, and will include the branches' facilities and associated loan and deposit accounts. The offices will be operated as branches of Capital State Bank, Inc. Total deposits of the branches approximated $46.5 million and total loans approximated $11 million as of December 31, 1998. Under the terms of the purchase agreement, Capital State will assume the deposits and acquire the loans of the branch offices. The total consideration to be paid is anticipated to be approximately $3.4 million and will be finally determined at closing based upon the total deposits assumed plus the seller's net book value of the branch offices and equipment.

During 1998, the Company applied for and on January 25, 1999 received preliminary approval from the Office of the Comptroller of the Currency to begin organizing a new subsidiary bank, Shenandoah Valley National Bank, to be located in Winchester, Virginia. This newly chartered institution will be initially capitalized with $4 million, to be funded by a special dividend in the amount of $3 million from the Company's subsidiary bank, South Branch Valley National Bank, and from a $1 million term loan from an unaffiliated bank. Shenandoah Valley National Bank is expected to open in May 1999 pending final regulatory approvals.

NOTE 15. SUBSEQUENT EVENT

On March 22, 1999, the Company entered into a letter of intent ("Letter") to affiliate with Potomac Valley Bank ("Potomac") in Petersburg, West Virginia. Under the terms of the Letter, South Branch and Potomac propose a merger whereby the shareholders of Potomac would exchange all of their outstanding shares of common stock for shares of South Branch common stock at a book-for-book exchange based on the respective book values of South Branch and Potomac as of the closing date. At December 31, 1998, the exchange ratio would have been 3.2143 shares of South Branch common stock for each share of Potomac's 90,000 outstanding shares of common stock. The terms of the Letter also include, among others, that the merger is subject to negotiation of a definitive merger agreement, South Branch changing its name to a name mutually agreeable to both parties, and approval of the transaction by all applicable regulatory authorities and the shareholders of South Branch and Potomac. It is expected that the transaction will be accounted for using the pooling of interests method of accounting. As of December 31, 1998, Potomac's assets, loans, deposits and shareholders' equity totaled $94,297,000, $50,393,000, $81,968,000 and $11,813,000, respectively.

NOTE 16. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following summarizes the methods and significant assumptions used by the Company in estimating its fair value disclosures for financial instruments.

CASH AND DUE FROM BANKS: The carrying values of cash and due from banks approximate their estimated fair value.

INTEREST BEARING DEPOSITS WITH OTHER BANKS: The fair values of interest bearing deposits with other banks are estimated by discounting scheduled future receipts of principal and interest at the current rates offered on similar instruments with similar remaining maturities.

FEDERAL FUNDS SOLD: The carrying values of Federal funds sold approximate their estimated fair values.

SECURITIES: Estimated fair values of securities are based on quoted market prices, where available. If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable securities.

LOANS: The estimated fair values for loans are computed based on scheduled future cash flows of principal and interest, discounted at interest rates currently offered for loans with similar terms to borrowers of similar credit quality. No prepayments of principal are assumed.

ACCRUED INTEREST RECEIVABLE AND PAYABLE: The carrying values of accrued interest receivable and payable approximate their estimated fair values.

DEPOSITS: The estimated fair values of demand deposits (i.e. non interest bearing checking NOW, Super NOW, money market and savings accounts) and other variable rate deposits approximate their carrying values. Fair values of fixed maturity deposits are estimated using a discounted cash flow methodology at rates currently offered for deposits with similar remaining maturities. Any intangible value of long-term relationships with depositors is not considered in estimating the fair values disclosed.

SHORT-TERM BORROWINGS: The carrying values of short-term borrowings approximate their estimated fair values.

LONG-TERM BORROWINGS: The fair values of long-term borrowings are estimated by discounting scheduled future payments of principal and interest at current rates available on borrowings with similar terms.

OFF-BALANCE SHEET INSTRUMENTS: The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit standing of the counterparties. The amounts of fees currently charged on commitments and standby letters of credit are deemed insignificant, and therefore, the estimated fair values and carrying values are not shown below.

The carrying values and estimated fair values of the Company's financial instruments are summarized below:

	December 31, 1998		December 31, 1997	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial assets:				
Cash and due from banks	$4,239,721	$4,239,721	$3,945,099	$3,945,099
Interest bearing deposits, other banks	770,000	770,000	1,256,000	1,283,843
Investment in affiliate	-	-	5,273,481	5,273,481
Federal funds sold	4,842,745	4,842,745	5,806,717	5,806,717
Securities available for sale	31,409,924	31,409,924	27,547,094	27,547,094
Loans	142,770,127	145,033,585	92,572,652	93,668,853
Accrued interest receivable	1,059,990	1,059,990	864,083	864,083
	$185,092,507	$187,355,965	$137,265,126	$138,389,170
Financial liabilities:				
Deposits	$146,373,192	$147,586,412	$106,984,797	$107,728,110
Short-term borrowings	4,644,143	4,644,143	7,145,010	7,145,000
Long-term borrowings	16,468,875	16,468,875	10,395,848	10,395,848
Accrued interest payable	677,171	677,171	483,857	483,857
	$168,163,381	$169,376,601	$125,009,512	$125,752,815

Note 17. Condensed Financial Statements of Parent Company

The investment of the Company in its wholly-owned subsidiaries is presented on the equity method of accounting. Information relative to the Company's balance sheets at December 31, 1998 and 1997, and the related statements of income and cash flows for the years ended December 31, 1998, 1997 and 1996, are presented as follows:

Balance Sheets

	1998	1997
Assets		
Cash and due from banks	$ 223,555	$ 145,593
Investment in bank subsidiaries, eliminated in consolidation	23,388,502	12,189,418
Securities available for sale	306,625	206,625
Investment in affiliate	-	5,273,481
Furniture and equipment	125,966	
Other assets	100,481	109,374
Total assets	$24,145,129	$17,924,491
Liabilities and Shareholders' Equity		
Long-term borrowings	$ -	$ 2,837,500
Other liabilities	-	26,439
Total liabilities	-	2,863,939
Common stock, $2.50 par value, authorized 1998-2,000,000 shares, 1997-600,000 shares; issued 1998-600,407 shares, 1997-416,942 shares	1,501,018	1,042,355
Capital surplus	9,611,774	2,089,709
Retained earnings (consisting of undivided profits of bank subsidiaries not yet distributed)	13,103,264	11,898,420
Less cost of shares acquired for the treasury 1998-9,115 shares; 1997-4,115 shares	(384,724)	(166,970)
Accumulated other comprehensive income	313,797	197,038
Total shareholders' equity	24,145,129	15,060,552
Total liabilities and shareholders' equity	$24,145,129	$ 17,924,491

Statements of Income

	1998	1997	1996
Income			
Dividends from bank subsidiaries	$1,300,000	$1,500,000	600,000
Other dividends and interest income	7,454	9,225	2,797
Management fees from bank subsidiaries	55,000	-	-
Securities gains	4,110	-	-
Total income	1,366,564	1,509,225	602,797
Expense			
Interest expense	56,689	214,790	-
Operating expenses	184,057	65,400	26,504
Total expenses	240,746	280,190	26,504
Income before income taxes and equity in undistributed income of bank subsidiaries	1,125,818	1,229,035	576,293
Income tax (benefit)	(72,200)	(107,874)	(10,204)
Income before equity in undistributed income of bank subsidiaries	1,198,018	1,336,909	586,497
Equity in undistributed income of bank subsidiaries	535,276	182,748	903,540
Net income	$1,733,294	$1,519,657	$ 1,490,037

Statements of Cash Flows

	1998	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$1,733,294	$1,519,657	$1,490,037
Adjustments to reconcile net earningsto net cash provided by operating activities:			
Equity in undistributed net income of bank subsidiaries	(535,276)	(182,748)	(903,540)
Depreciation	1,396	-	-
Securities gains	(4,110)	-	-
(Increase) decrease in other assets	8,893	(96,170)	(6,377)
Increase (decrease) in other liabilities	(26,439)	26,439	-
Net cash provided by operating activities	1,177,758	1,267,178	580,120
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from sales of securities available for sale	204,110	-	-
Purchases of securities available for sale	(300,000)	-	(200,000)
Purchase of common stock of affiliate	(90,465)	(5,273,481)	-
Purchases of furniture and equipment	(127,363)	-	-
Net cash (used in) investing activities	(313,718)	(5,273,481)	(200,000)
CASH FLOWS FROM FINANCING ACTIVITIES			
Dividends paid to shareholders	(528,450)	(332,705)	(291,453)
Net proceeds from common stock sold	-	1,489,968	-
Purchase of treasury stock	(217,754)	-	-
Proceeds from long-term borrowings	-	3,500,000	-
Repayment of long-term borrowings	(39,874)	(662,500)	-
Net cash provided by (used in) financing activities	(786,078)	3,994,763	(291,453)
Increase (decrease) in cash	77,962	(11,540)	88,667
Cash:			
Beginning	145,593	157,133	68,466
Ending	$ 223,555	$ 145,593	$ 157,133
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Cash payments for:			
Interest	$ 83,128	$ 188,351	$ -
SUPPLEMENTAL SCHEDULE OF NONCASH FINANCING ACTIVITIES			
Issuance of 183,465 shares of Company common stock in connection with acquisition of Capital State Bank, Inc.	$7,980,728	$ -	$ -
Long-term borrowings transferred to bank subsidiary	$2,797,626	$ -	$ -

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

There has been no Form 8-K filed within 24 months prior to the date of the most recent financial statements reporting a change of accountants and/or reporting disagreements on any matter of accounting principle or financial statement disclosure.

PART III.

ITEM 9. DIRECTORS AND EXECUTIVE OFFICERS

Information required by this item is set forth under the captions "NOMINEE FOR DIRECTOR WHOSE TERM WILL EXPIRE IN 2001", "NOMINEES FOR DIRECTORS WHOSE TERMS EXPIRE IN 2002", "DIRECTORS WHOSE TERMS EXPIRE IN 2000" and "DIRECTORS WHOSE TERMS EXPIRE IN 2001" on pages 7 through 11, and under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" on page 3 of South Branch's 1999 Proxy Statement, and is incorporated herein by reference.

ITEM 10. EXECUTIVE COMPENSATION

Information required by this item is set forth under the caption"EXECUTIVE COMPENSATION" on pages 13 through 15, and under the caption "Fees and Benefit Plans for Directors" on page 5 of South Branch's 1999 Proxy Statement, and is incorporated herein by reference.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Information required by this item is set forth under the caption "Security Ownership of Directors and Officers" on page 6, and under the captions "NOMINEE FOR DIRECTOR WHOSE TERM WILL EXPIRE IN 2001", "NOMINEES FOR DIRECTORS WHOSE TERMS EXPIRE IN 2002", "DIRECTORS WHOSE TERMS EXPIRE IN 2000" and "DIRECTORS WHOSE TERMS EXPIRE IN 2001" on pages 7 through 11, of South Branch's 1999 Proxy Statement, and is incorporated herein by reference.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information required by this item is set forth under the captions "Related Transactions" on page 4 of South Branch's 1999 Proxy Statement, and is incorporated herein by reference.

ITEM 13. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

All financial statements and financial statement schedules required to be filed by this Form or by Regulation S-X, which are applicable to the registrant, have been presented in the financial statements and notes thereto in Item 7 in management's discussion and analysis of financial condition and results of operation in Item 6 or elsewhere in this filing where appropriate. The listing of exhibits follows:

INDEX TO EXHIBITS

A. Exhibits

Exhibit or Filing Number Reference	Description	Page(s) in Form 10-KSB Prior
(3)	Articles of Incorporation and By-laws	
	(i) Articles of Association of South Branch Valley National Bank	(a)
	(ii) Articles of Incorporation of South Valley Bancorp, Inc., amended and restated April 1998	(c)
	(iii) By-laws of South Branch Valley Bancorp, Inc.	(a)
(10)	Material Contracts	
	(i) Change of Control Agreement	(b)
	(ii) Employment Agreement	57
	(iii) 1998 Officers Stock Option Plan	(c)
(21)	Subsidiaries of the Registrant	68
(23)	Consent of Independent Auditors	69
(27)	Financial Data Schedule -- electronic filing only	

(a) Incorporated herein by reference to exhibits to South Branch Valley Bancorp, Inc.'s registration statement on Form S-4 dated September 1, 1987, Registration No. 33-16947 filed on or about September 1, 1987.

(b) Incorporated herein by reference to exhibits to South Branch Valley Bancorp, Inc.'s Form 10-KSB for the fiscal year ended December 31, 1995 filed on or about March 22, 1996.

(c) Incorporated herein by reference to exhibits to South Branch Valley Bancorp, Inc.'s Form 10-QSB for the quarter ended June 30, 1998 filed on or about August 17, 1998.

B. Reports on Form 8-K

No reports of Form 8-K were filed by the registrant during the fourth quarter of the year ended December 31, 1998.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOUTH BRANCH VALLEY BANCORP, INC.
a West Virginia Corporation
(registrant)

By: /s/Oscar M. Bean 3/30/99	By:/s/ H. Charles Maddy, III 3/30/99
Oscar M. Bean Date Chairman of the Board	H. Charles Maddy, III Date President & Chief Executive Officer

By: /s/Robert S. Tissue 3/30/99

Robert S. Tissue Date
Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

	Title	Date
/s/ Oscar M. Bean Oscar M. Bean	Director	March 30, 1999
Frank A. Baer, III	Director	
Donald W. Biller	Director	
/s/ James M. Cookman James M. Cookman	Director	March 30, 1999
John W. Crites	Director	
Georgette Rashid George	Director	
/s/ Thomas J. Hawse, III Thomas J. Hawse, III	Director	March 30, 1999
/s/ Phoebe Fisher Heishman Phoebe Fisher Heishman	Director	March 30, 1999

SIGNATURES - continued

	Title	Date
- -------------- Gary L. Hinkle	Director	
- -------------- Jeffrey E. Hott	Director	
/s/ H. Charles Maddy, III - ---------------------------- H. Charles Maddy, III	Director	March 30, 1999
/s/ Harold K. Michael - ----------------------------- Harold K. Michael	Director	March 30, 1999
/s/ Ronald F. Miller - ----------------------------- Ronald F. Miller	Director	March 30, 1999
/s/ Russell F. Ratliff, Jr. - ----------------------------- Russell F. Ratliff, Jr.	Director	March 30, 1999
- ----------------------------- Charles S. Piccirillo	Director	
/s/ Harry C. Welton, Jr. - ----------------------------- Harry C. Welton, Jr.	Director	March 30, 1999

Exhibit 10 (ii)

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (this "Agreement") made in duplicate originals and effective this 1st day of August, 1998, is between SOUTH BRANCH VALLEY BANCORP, INC., a West Virginia corporation and bank holding company (the "Company"), and RONALD MILLER ("Employee").

WHEREAS, the Company is forming a subsidiary entity (the "Virginia Bank") for purposes of conducting banking operations in the Commonwealth of Virginia; and

WHEREAS, the Company offers the terms and conditions of employment hereinafter set forth and the Employee has indicated his willingness to accept such terms and conditions in consideration of his employment with the Company.

NOW, THEREFORE, in consideration of the mutual promises and covenants made in this Agreement, the parties agree as follows:

1. EMPLOYMENT. The Company hereby employs Employee and Employee hereby accepts employment with the Company as President, Chief Executive Officer and Chairman of the Board of Directors of the Virginia Bank and member of the Board of Directors of the Company upon the terms and conditions set forth herein.

2. TERM. The term of this Agreement shall be for three (3) years, unless one of the parties terminates this Agreement as provided herein. The Board of Directors of the Company shall review the Agreement at least annually, and may, with the consent of the Employee, extend this term of employment for additional one (1) year term(s), in which case such term shall end one (1) year from the date on which it is last renewed.

3. DUTIES. Employee shall perform and have all of the duties and responsibilities that may be assigned to him from time to time by the Board of Directors of the Company. Employee shall devote his best efforts on a full-time basis to the performance of such duties.

4. COMPENSATION AND BENEFITS. During the term of employment, the Company agrees to pay Employee a base salary and to provide benefits as set forth in Exhibit A, which is attached hereto and incorporated herein by reference.

5. TERMINATION BY THE COMPANY OR EMPLOYEE. The employment of Employee with the Company may be terminated by any one of the following means, in which case Employee shall be entitled to such compensation as is described below:

A. Mutual Agreement: The Employee's employment may be terminated by mutual agreement of the parties upon such terms and conditions as they may agree.

B. For Cause.

(1) The Employee's employment may be terminated by the Company for cause consisting of one or more of the reasons specified in Paragraph 5(B)(2)(a) - (e) below; provided, however, that if the cause of termination is for a reason specified in Paragraph 5(B)(2)(a) below, and if in the reasonable judgment of the Board of Directors of the Company the damage incurred by the Company as a result of Employee's conduct constituting cause is damage of a type that is capable of being substantially reversed and corrected, the Company shall give Employee thirty (30) days advance notice of the Company's intention to terminate his employment for cause and a reasonable opportunity to cure the cause of the possible termination to the satisfaction of the Company.

(2) For purposes of this Agreement, the term "cause" shall be defined as follows:

(a) Employee's repeated negligence, malfeasance or misfeasance in the performance of Employee's duties that can reasonably be expected to have an adverse impact upon the business and affairs of the Company;
(b) Employee's commission of any act constituting theft, intentional wrongdoing or fraud;
(c) The conviction of the Employee of a felony criminal offense in either state or federal court;
(d) Any single act by Employee constituting gross negligence or which causes material harm to the reputation, financial condition or property of the Company; or
(e) The death of Employee during the term of this Agreement, in which event the Company shall pay to the estate of the Employee any compensation for services rendered but unpaid prior to the Employee's date of death.

(3) The Board of Directors of the Company shall determine, in its sole discretion, whether any acts and/or omissions on the part of Employee constitute "cause" as defined above. Notwithstanding the foregoing, Employee shall be entitled to arbitrate a finding of the Board of Directors of "cause" in accordance with Paragraph 9 hereof.

(4) In the event that Company terminates Employee's employment for cause as defined above, Employee shall be entitled to be paid his regular salary and benefits up to the effective date of the termination, but not any additional compensation.

C. Not for Cause. Employee's employment may be terminated by the Company for any reason permitted under applicable law so long as Employee is given thirty (30) days advance written notice (or payment in lieu thereof). In the event of a termination pursuant to this subparagraph, Employee shall be entitled to payment from the Company equivalent to the base salary compensation set forth in this Agreement for the remaining term of the Agreement or severance pay equal to six (6) months of base salary payments, whichever is greater.

D. Employee Resignation. Employee recognizes and understands the vital role he plays in the Company's establishment of the Virginia Bank, and therefore agrees not to resign from employment during the initial three-year term of this Agreement except in the event of his disability. If the Employee resigns in violation of this commitment, Employee agrees to comply with the restrictions set forth in Paragraph 6 below.

E. Change in Control. Exhibit B hereto sets forth the rights and responsibilities of the parties in the event of a change in control, as defined therein, and is incorporated herein by reference.

F. No Charter or Branch. In the event that (1) employment of Employee as set forth herein is not approved by the regulatory authorities or (2) the Company is rendered unable either by lack of regulatory approval or by business impracticability to establish operations in the City of Winchester, County of Frederick, Virginia either by way of the formation and charter of the Virginia Bank or the establishment of a branch bank, the Company and Employee agree that this Agreement shall terminate as of the date upon which such fact(s) become(s) reasonably apparent. The parties further agree that each shall hold the other harmless in any such event.

6. NONCOMPETITION AND NONSOLICITATION. In consideration of the covenants set forth herein, including but not limited to the severance pay set forth in Paragraph 5(E) and Exhibit A, Employee agrees as follows:

A. For a period of five (5) years after Employee's employment with the Company is terminated by Employee for any reason other than Employee's disability, Employee shall not, directly or indirectly, engage in the business of banking in the City of Winchester or the County of Frederick, Virginia. For purposes of this Paragraph 6(A), being engaged in the business of banking shall mean Employee's presence or work in a bank office in the specified geographic area or Employee's solicitation of business from clients with a primary or principle office in the specified geographic area.

B. During Employee's employment by the Company and for five (5) years after Employee's employment with the Company is terminated by Employee for any reason other than Employee's disability, Employee shall not, on his own behalf or on behalf of any other person, corporation or entity, either directly or indirectly, solicit, induce, recruit or cause another person in the employ of the Company or its affiliates to terminate his or her employment for the purpose of joining, associating or becoming an employee with any business which is in competition with any business or activity engaged in by the Company or its affiliates.

C. Employee further recognizes and acknowledges that in the event of the termination of Employee's employment with the Company for any reason other than Employee's disability, (1) a breach of the obligations and conditions set forth herein will irreparably harm and damage the Company; (2) an award of money damages may not be adequate to remedy such harm; and (3) considering Employee's relevant background, education and experience, Employee believes that he will be able to earn a livelihood without violating the foregoing restrictions. Consequently, Employee agrees that, in the event that Employee breaches any of the covenants set forth in this Paragraph 6, the Company and/or its affiliates shall be entitled to both a preliminary and permanent injunction in order to prevent the continuation of such harm and to recover money damages, insofar as they can be determined, including, without limitation, all costs and attorneys' fees incurred by the Company in enforcing the provisions of this Paragraph 6. Such relief may be sought notwithstanding the arbitration provision set forth in Paragraph 10 below.

7. DEFINITION OF DISABILITY. For purposes of the Agreement, the term "disability" shall mean a physical or mental condition rendering Employee substantially and permanently unable to perform the duties of an officer and director of a banking organization.

8. NOTICES. Any notice required or permitted to be given under this Agreement shall be sufficient if in writing and sent by registered or certified mail listed herein. In the case of Employee to the following address: Post Office Box 384, Strasburg, Virginia 22657. In the case of the Company to the President addressed to H. Charles Maddy, III in care of South Branch Valley Bancorp, Inc., P.O. Box 680, Moorefield, WV 26836. Any notice sent pursuant to this paragraph shall be effective when deposited in the mail.

9. CONFIDENTIAL INFORMATION. Employee shall not, during the term of this Agreement or at any time thereafter, directly or indirectly, publish or disclose to any person or entity any confidential information concerning the assets, business or affairs of the Company, including but not limited to any trade secrets, financial data, employee or customer/client information or organizational structure.

10. ARBITRATION. Any dispute between the parties arising out of or with respect to this Agreement or any of its provisions or Employee's employment with the Company shall be resolved by the sole and exclusive remedy of binding arbitration. Arbitration shall be conducted in Martinsburg, West Virginia in accordance with the rules of the American Arbitration Association ("AAA"). The parties agree to select one arbitrator from an AAA employment panel. The arbitration shall be conducted in accordance with the West Virginia Rules of Evidence and all discovery issues shall be decided by the arbitrator. The arbitrator shall supply a written opinion and analysis of the matter submitted for arbitration along with the decision. The arbitration decision shall be final and subject to enforcement in the local circuit court.

11. ENTIRE AGREEMENT. This Agreement constitutes the entire Agreement between the parties and shall supersede all prior agreements and understandings, both written and oral, among the parties with respect to the subject matter hereof, and may not be changed or amended except by an instrument in writing to be executed by each of the parties hereto.

12. SEVERABILITY. If any provision hereof, or any portion of any provision hereof, is held to be invalid, illegal or unenforceable, all other provisions shall remain in force and effect as if such invalid, illegal or unenforceable provision or portion thereof had not been included herein. If any provision or portion of any provision of this Agreement is so broad as to be unenforceable, such provision or a portion thereof shall be interpreted to be only so broad as is enforceable.

13. HEADINGS. The headings contained in this Agreement are included for convenience or reference only and shall have no effect on the construction, meaning or interpretation of this Agreement.

14. GOVERNING LAW. The laws of the State of West Virginia shall govern the interpretation and enforcement of this Agreement.

15. AMENDMENTS. Any amendments to the Agreement must be in writing and signed by all parties hereto except that extensions of the term of this Agreement under Paragraph 2 above, may be evidenced by minutes of a meeting of the Board of Directors.

16. WAVIER OF BREACH. No requirement of this Agreement may be waived except by a written document signed by the party adversely affected. A waiver of a breach of any provision of the Agreement by any party shall not be construed as a waiver of subsequent breaches of that provision.

17. COUNTERPARTS. This Agreement may be executed in counterparts, all of which shall be considered one and the same Agreement and each of which shall be deemed an original.

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed in its corporate name by its corporate officer thereunto duly authorized, and Employee has hereunto set his hand and seal, as of the day and year first above written:

SOUTH BRANCH VALLEY BANCORP, INC.

By: ___________________________________

Its: __________________________________

Ronald Miller

Exhibit A
Compensation and Benefits

A. Base Salary. Employee's starting base salary shall be $75,000 per year. As of the date that the Virginia Bank opens for business, the base salary shall be increased to $100,000 per year. Employee shall be considered for salary increases on the basis of merit beginning in the second year of his employment.

B. Bonus. In addition to the base salary provided for herein, Employee shall be eligible for incentive bonuses subject to goals and criteria to be determined by the Board of Directors of the Company.

C. Vacation. Employee shall be entitled to all paid vacation and holidays and other paid leave as provided by the Company to other employees.

D. Fringe Benefits. Except as specified below, the Company shall afford to Employee the benefit of all fringe benefits afforded to all other Company officers, including but not limited to retirement plans, stock ownership or stock option plans, life insurance, disability, health and accident insurance benefits or any other fringe benefit plan now existing or hereinafter adopted by the Company, subject to the terms and conditions thereof.
   (1) The Company shall pay 65% of the actual premiums paid by the Company for Employee's health and accident insurance benefits and Employee shall be responsible for the remaining 35% of the actual premiums.
   (2) The Company shall provide life insurance for the Employee in the amount of $100,000.

E. Business Expenses. The Company shall reimburse Employee for all reasonable expenses incurred by Employee in carrying out his duties and responsibilities, including but not limited to reimbursing civic club organization dues and reasonable expenses for customer entertainment.

F. Automobile. The Company shall purchase from Employee the 1996 Buick Ultra owned by him as of the execution of this Agreement and provide such vehicle for the employee's business and personal use. The purchase price of the vehicle shall be agreed upon between the Company's President and Employee. Following the purchase, the Company shall be responsible for expenses associated with the vehicle including but not limited to taxes, gasoline, licenses, maintenance, repair, insurance and reasonable cellular phone charges. Employee shall be subject to tax for his personal use of the vehicle in accordance with the Internal Revenue Code and any applicable state law. Upon approval of the Company, appropriate replacement vehicles may be provided in the future.

G. Director's Fees. The Company shall pay Employee the same director's fees as are provided to other inside officer members of the Board of Directors.

Exhibit B

Change in Control Agreement

A. Definitions. For purposes of this Exhibit B, the following definitions shall apply:

(1) "Change of Control" means

(a) a change of ownership of the Company that would have to be reported to the Securities and Exchange Commission as a Change of Control, including but not limited to the acquisition by any "person" and/or entity as defined by securities regulations and law, of direct or indirect "beneficial ownership" as defined, of twenty-five percent (25%) or more of the combined voting power of the Company's then outstanding securities; or

(b) the failure during any period of three (3) consecutive years of individuals who at the beginning of such period constitute the Board for any reason to constitute at least a majority thereof, unless the election of each director who was not a director at the beginning of such period has been approved in advance by directors representing at least two-thirds (2/3) of the directors at the beginning of the period; or

(c) the consummation of a "Business Combination" as defined in the company's Articles of Incorporation.

(2) "Salary" means the greater of $75,000 or the average of Employee's full earnings reported on IRS Form W-2 for the two full year periods immediately prior to the date of the consummation of the Change of Control or for the two full year periods immediately preceding the Date of Termination, whichever is greater.

(3) For purposes of this Exhibit B, "Good Cause" has the same meaning as the term "cause" set forth in Paragraph 5(B)(2) of the foregoing Employment Agreement.

(4) "Disability" means a physical or mental condition rendering Employee substantially unable to perform the duties of an officer and director of a banking organization.

(5) "Retirement" means termination of employment by Employee in accordance with Company's (or its successor's) retirement plan, including early retirement as approved by the Board of Directors.

(6) "Good Reason" means

(a) A Change of Control in the Company (as defined above) and:

(i) a decrease in Employee's Salary below its level in effect immediately prior to the date of consummation of the Change of Control, without Employee's prior written consent; or

(ii) a material reduction in the importance of Employee's job responsibilities or assignment of job responsibilites inconsistent with employee's responsibility prior to the Change in Control without Employee's prior written consent; or

(iii) a geographical relocation of Employee to an office more than 20 miles from Employee's location at the time of the Change of Control or the imposition of travel requirements inconsistent with those existing prior to the Change in Control without Employee's prior written consent; or

(b) Failure of the Company to obtain assumption of this Change in Control Agreement by its successor as required by Paragraph E(1) below; or

(c) Any removal of Employee from, or failure to re-elect Employee to any of Employee's positioins with Company immediately prior to a Change in Control (except in connection with the termination of Employee's employment for Good Cause, death, Disability or Retirement) without Employee's prior consent.

(7) "Wrongful Termination" means termination of Employee's employment by the Company or its affiliates for any reason other than at Employee's option, Good Cause or the death, Disability or Retirement of Employee prior to the expiration of eighteen (18) months after consummation of the Change of Control.

B. Compensation of Employee Upon Termination for Good Reason or Wrongful Termination within Twenty-four (24) Months of a Change in Control. Except as hereinafter provided, if Employee terminates his employment with the Company for Good Reason or the Company terminates Employee's employment in a manner constituting Wrongful Termination, the Company agrees as follows:

(1) The Company shall pay Employee a cash payment equal to Employee's Salary, on a monthly basis, multiplied by the number of months between the Date of Termination and the date that is eighteen (18) months after the date of consummation of the Change of Control.

(2) For the year in which termination occurs, Employee will be entitled to receive his reasonable share of the Company's cash bonuses, if any, allocated in accordance with existing principles and authorized by the Board of Directors. The amount of Employee's cash incentive award shall not be reduced due to Employee not being actively employed for the full year.

(3) Employee will continue to participate, without discrimination, for the number of months between the Date of Termination and the date that is eighteen (18) months after the date of the consummation of the Change of Control in benefit plans (such as retirement, disability and medical insurance) maintained after any Change of Control for employees, in general, of the Company, or any successor organization, provided Employee's continued participation is possible under the general terms and conditions of such plans. In the event Employee's participation in any such plan is barred, the Company shall arrange to provide Employee with benefits substantially similar to those which Employee would have been entitled had his participation not been barred. However, in no event will Employee receive from the Company the employee benefits contemplated by this subparagraph if Employee receives comparable benefits from any other source.

(4) In the event Employee becomes entitled to any payments or benefits under this Change in Control Agreement or any benefit plan or program of the Company, if any such payments or benefits will be subject to the tax (the "Excise Tax") imposed by Section 4999 of the Internal Revenue Code of 1986, as amended (or any similar tax that may hereinafter be imposed), the Company shall pay to employee an additional amount or amounts (each, a "Gross Up Payment"), such that the net amount or amounts retained by Employee, after deduction of any Excise Tax on any of the above-described payments or benefits and any federal, state and local income tax and excise tax upon payment provided for by this section, shall be equal to the amount of such payment or benefits prior to the imposition of such Excise Tax.

(5) Paragraph 6 (Noncompetition and Nonsolicitation) of the foregoing Agreement shall not apply.

C. Other Employment. Employee shall not be required to mitigate the amount of any payment provided for in this Change in Control Agreement by seeking other employment. The amount of any payment provided for in this Change in Control Agreement shall not be reduced by any compensation earned or benefits provided (except as set forth in Paragraph B(3) above) as the result of employment by another employer after the Date of Termination.

D. Rights of Company Prior to the Change of Control. This Change in Control Agreement shall not effect the right of the Company or Employee to terminate the foregoing Agreement or the employment of Employee in accordance thereof; provided, however, that any termination or reduction in salary or benefits that takes place after discussions have commenced that result in a Change in Control shall be presumed (without clear and convincing evidence to the contrary) to be a violation of this Change in Control Agreement entitling Employee to the benefits hereof, so that any termination by Company shall be deemed to be a wrongful termination, and all references in this Change in Control Agreement to Salary shall be deemed to mean the Salary, as defined herein, based on the earnings Employee would have had prior to any reduction thereof.

E. Successors; Binding Agreement.

(1) The Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company, by agreement in form and substance satisfactory to Employee, to expressly assume and agree to perform this Change in Control Agreement. Failure of the Company to obtain such agreement prior to the effectiveness of any such succession shall be a breach of the this Change in Control Agreement and shall entitle Employee to compensation from the Company in the same amount and on the same terms as he would be entitled to hereunder if he terminated his employment for Good Reason hereunder.

(2) This Change in Control Agreement and all rights of Employee hereunder shall inure to the benefit of and be enforceable by Employee's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees, and legatees. If Employee should die while any amounts would still be payable to him hereunder if he had continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Agreement to Employee's devisee, legatee, or other designee or, if there be no such designee, to Employee's estate

Exhibit 21

SUBSIDIARIES OF REGISTRANT

The following lists the subsidiary of the registrant, a West Virginia Corporation.

South Branch Valley National Bank, a national banking association organized under the laws of the United States of America

Capital State Bank, a state banking association organized under the laws of the State of West Virginia

Exhibit 23

CONSENT OF INDEPENDENT AUDITORS

Securities and Exchange Commission
Washington, D.C.

We hereby consent to the inclusion in this Annual Report on Form 10-KSB of our report dated February 11, 1999, except for Note 15 as to which the date is March 22, 1999, on our audit of the consolidated financial statements of South Branch Valley Bancorp, Inc. as of December 31, 1998 and 1997, appearing in Part II, Item 7 of the 1998 Form 10-KSB of South Branch Valley Bancorp, Inc.

ARNETT & FOSTER, P.L.L.C.

/s/Arnett & Foster, P.L.L.C.

Charleston, West Virginia
March 30, 1999

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South Branch Valley Bancorp

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